



Report on Govt. Purchasing in
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MINISTER OF STATE, PRIVY COUNCIL OFFICE

PRIME MINISTER

GOVERNMENT PURCHASING

The 1983 Efficiency Programme included a multi-department review of Contract and Procurement Procedures. Scrutinies were carried out in nine separate departments, and the review was co-ordinated by a small central team in the Cabinet Office (MPO). I commend the very thorough job that has been done.

... I attach the central team's report, and a summary of their main findings and recommendations. But I strongly suggest that you read the full report: it makes interesting reading.

MAIN CONCLUSIONS

The team recommend radical changes in departments' whole approach to buying. They believe that rigorous implementation of their recommendations across the whole of government non-warlike purchasing could result in savings of well over £400 million, or 5% of the current annual spend both on goods and services and on the administration of purchasing.

Some savings will come from streamlining procedures, reducing paperwork and cutting out unnecessary double-checking. Some will come from identifying and reducing the on-costs of procurement (particularly storage and distribution). The major savings, however, will come from getting down the prices government pays for the goods and services it buys. To achieve this the team recommends that departments:

- plan and organise purchasing in a way that will enable them to make fuller use of the government's considerable purchasing power
- establish closer liaison with suppliers and place greater reliance on their ability and resourcefulness to meet government needs in the most cost-effective way;
- use specifications which enable government to buy what is good enough for the job rather than the best possible.

These approaches will not only help government to get better value for money; they should also stimulate greater competitiveness in British industry.

Departments need to take steps to clarify the responsibilities of staff in the procurement process. The report recommends thorough training in buying methods; and the introduction of performance indicators and incentives.

MANAGEMENT IN CONFIDENCE

CABINET OFFICE
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Government Purchasing

Report to the Prime Minister
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LIST OF ABBREVIATIONS

AP (Division)	Commercial Accounting, Contracts and Purchasing Policy (Division)
BS	British Standard
BSI	British Standards Institution
CCTA	Central Computer and Telecommunications Agency
Cmnd	Command Paper
COI	Central Office of Information
CPU	Central Purchasing Unit
DHSS	Department of Health and Social Security
DIN	Deutsches Institut für Normung (West German Standard)
DOE	Department of the Environment
DTI	Department of Trade and Industry
EC	European Community
EO	Executive Officer
FCO	Foreign and Commonwealth Office
FMI	Financial Management Initiative
GATT	General Agreement on Tariffs and Trade
HEO	Higher Executive Officer
HMSO	Her Majesty's Stationery Office
HMT	Her Majesty's Treasury
IPS	Institute of Purchasing and Supply
MOD	Ministry of Defence
MPO	Management and Personnel Office
NATO	North Atlantic Treaty Organisation
NEDO	National Economic Development Office
NHS	National Health Service
ODA	Overseas Development Administration
PPI	Public Purchasing Initiative
PSA	Property Services Agency
SVOC	Small Value Order Cells
UK	United Kingdom
US	United States

CHAPTER 1: INTRODUCTION

1.1 The 1983 Efficiency Programme included a multi-department review of government contract and procurement procedures. Our report sets out the main findings and makes recommendations aimed at:

- ensuring clear responsibilities for purchasing;
- establishing more efficient procedures for purchasing; and
- obtaining better value for money in what government buys.

1.2 Government departments need to buy certain goods and services to carry out their business. Procurement provides the means of meeting these needs from external sources of supply.

1.3 All departments have a procurement organisation. In a small department, where the main requirements are for stationery and office requisites, procurement may be the responsibility of the Clerk of Stationery or the Office Services Division. At the other end of the scale the procurement organisation may be large, such as the Ministry of Defence's formal Procurement Executive, and/or diffuse, such as the many Home Office units with authority to purchase locally.

1.4 The procurement organisation has two primary objectives:

- to provide end-users with what they need, when they need it, at the lowest cost; and
- to provide the Accounting Officer, and through him Parliament and the taxpayer, with value for money from expenditure on procurement.

These objectives should not conflict if the purchasing process is properly organised.

1.5 It is estimated that central government departments spent around £14,900 million* on goods and services in 1982. Of this, £7,300 million was spent by MOD on warlike equipment. This is subject to a separate study by MOD this year and was thus not included in our review. Around 12 per cent of all central government departments' expenditure on goods and services is spent through the central agencies (HMSO, CCTA, COI, Crown Suppliers, PSA).

1.6 Government buys a wide range of goods and services, for example, paper, vehicles, large computer installations and roads. Unit costs vary widely: computer tape head cleaners are ten a penny while a major computer installation such as the DHSS local office project can cost as much as £700 million over a number of years. Within this broad range there are some groups of goods and services on which government spends in aggregate more than £100 million a year; for example, travel and subsistence and Post Office, GIRO and bank charges.

*Excluding expenditure on the wages, salaries and employers' national insurance contributions of government purchasing staff; and including gross domestic fixed capital formation. Source: Central Statistical Office.

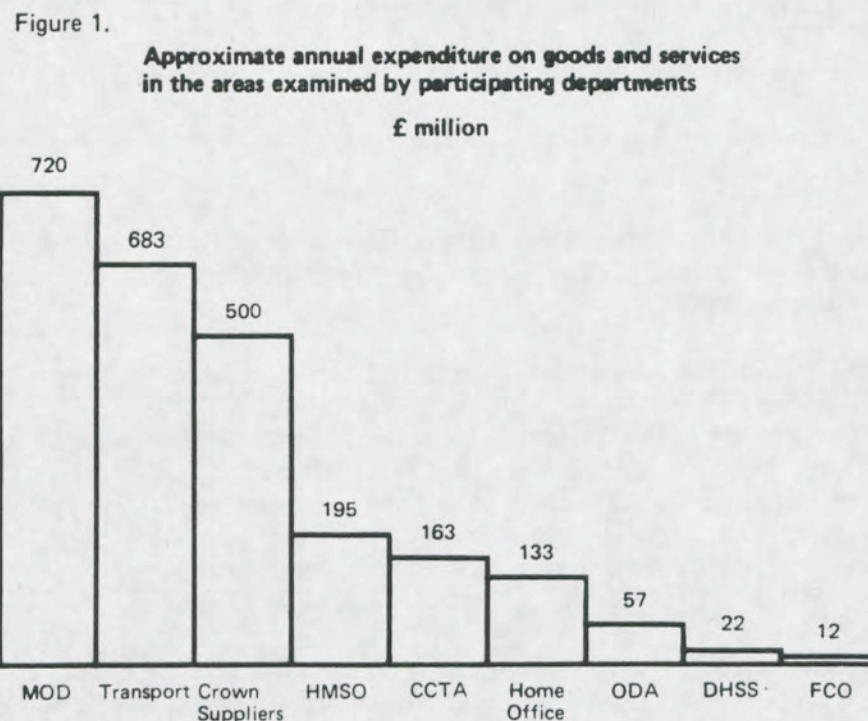
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1.7 The review's terms of reference were:

"To examine critically the procedures and organisations by means of which the procurement of a sample of goods, services and works is undertaken, monitored and controlled by government departments; and to make recommendations to improve the efficiency and effectiveness of such procedures and organisations both in the areas examined and, as appropriate, more widely."

1.8 Nine departments took part in the review (Defence, Transport, Crown Suppliers, Her Majesty's Stationery Office, Central Computer and Telecommunications Agency, Home Office, Overseas Development Administration, Department of Health and Social Security, and the Foreign and Commonwealth Office). They appointed examining officers to carry out scrutinies of specific areas of purchasing. Of the £7,600 million spent by central government departments on goods and services (excluding MOD warlike equipment, the NHS and other central government bodies), the review examined expenditure of around £2,500 million and the work of several thousand staff.

Figure 1 shows the coverage by participating department:



Departments buy some goods and services using call-off contracts arranged by another department. Expenditure on these goods and services is allocated in figure 1 to the department responsible for letting the contract.

Conduct of the review

1.9 Examining officers used the scrutiny technique. In particular they went to see the work being done to question those involved in buying. They visited a sample of suppliers to get their views on government buying practice. They also visited a range of private sector companies and nationalised industries to find out how they buy goods and services.

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1.10 The review involved much hard work by the examining officers and their helpers. It also involved much time on the part of officials carrying out purchasing who willingly explained to examining officers their work, problems and ideas. We are grateful to all who contributed their time and effort to this review and to the departmental studies. Annex A lists those who discussed aspects of the review with us.

Cost of review

1.11 The central part of the review cost around £75,000. The individual studies cost in total around £225,000, excluding the time of staff consulted in departments.

Findings of examining officers

1.12 Examining officers identified ways in which departments could reduce the costs of procurement and achieve further savings through getting keener prices. Details of their recommendations, and of the savings estimated to result from them, are in Annex B.

Central team findings

1.13 Our main finding is that the overall costs of acquiring non-warlike goods and services can be reduced substantially by a combination of a number of changes in government purchasing and supply procedures. We propose that departments set specific targets to reduce these costs within three years. Applied to all non-warlike government purchasing we believe that savings of over £400 million a year are achievable. This represents over five per cent of the annual expenditure on goods and services.

1.14 Some savings will flow from streamlining purchasing arrangements. Some will come through a more effective supply process, particularly through reductions in storage and distribution costs. In addition, price savings will be achieved by co-operation with industry through better planning of purchasing, through closer liaison between purchaser and supplier and through ensuring that specifications are better tuned to what the market can provide. We believe that our recommendations will help government obtain better value for money and, at the same time, help industry become more competitive. Our conclusions confirm the principles of the Public Purchasing Initiative (PPI) launched in 1980 to improve the competitiveness of industry and should help the operation of it in practice.

1.15 Our findings show the importance of implementing the principles underlying the Financial Management Initiative (FMI) to all activities in departments.¹ We identify the need to clarify responsibilities, to delegate appropriately, to make available the necessary information and to provide proper training for purchasing staff. Implementing our recommendations will thus make a practical contribution to the development of the FMI and will show how application of its principles can result in greater effectiveness.

1.16 Examining officers praised the hard work of departmental procurement staff. We endorse that from our own impressions gained on visits with examining officers. Generally, procurement staff at all levels do the job they are asked to do diligently. However, it is implicit in many of our recommendations that at present they are often not given the right job to do. Many of them are aware of the limitations of government procurement and some have themselves proposed ways of improving value for money. Many are keen to take on broader responsibility for securing greater value for money.

¹ *Efficiency and Effectiveness in the Civil Service* Cmnd 8616, HMSO, 1982.

The central report

1.17 This report is about getting better value for money. A wide range of factors influence value for money in procurement. The "money" involved is the total of the price paid, the cost of the procurement itself, and any other on-costs (storage and distribution, consumables, spares and maintenance, servicing, replacement etc). Quality is an equally important consideration which may be reflected in direct costs. A full list of the factors relevant to value for money in procurement is shown in the Public Purchasing Policy Guidelines published by the Treasury in 1981. These are reproduced at Annex C.

1.18 Our report examines in turn a range of factors that influence the value for money obtained by government departments in procurement. Chapters 2, 3 and 4 deal with the specification of what is needed, the process of securing a supplier and a price, and the conclusion of a suitable contract. Chapter 5 covers the administration of procurement. In each of these chapters we assess the evidence of the departmental examining officers and recommend changes directed at helping departments reduce the overall costs of procurement. In Chapter 6 we examine how to increase the effectiveness of government purchasing by improving the performance of staff. Chapter 7 considers how the changes we identify can be carried through at all levels in the purchasing and supply organisations of departments. Finally in Chapters 8 and 9 we consider the implications of our proposals for the three central procurement agencies which took part in the review and for government policies relating to procurement.

CHAPTER 2: DEFINING THE REQUIREMENT

2.1 The first step in the purchasing process is to decide what to buy. End-users are responsible and accountable for achieving a range of operational objectives. Thus they must be responsible for specifying the goods and services they need in order to achieve these objectives effectively.

2.2 The ODA report gives an example of what can go wrong if responsibility for specifying the requirement is taken away from the end-user:

- in issuing invitations to tender for a fisheries project in the Sudan, the Crown Agents disregarded specifications drawn up by the ODA project leader in the Sudan and substituted their own. As a result, a cold store - an integral part of the project - failed to cope with the tropical climate.

2.3 The HMSO report gives an example of what can happen when responsibilities are unclear:

- a recent HMSO review found that less expensive paper qualities were likely to be suitable for 85 per cent of print jobs reviewed. Using those, subject to their acceptability to end-users, would cost nearly 12 per cent less, a saving of the order of £400,000 a year.

Here, the end-users (in departments) seemed unaware of their responsibility, in the light of appropriate technical advice, to determine the quality of the paper used for departmental publications and hence the costs of them. We believe that this is because departments are not clear about the relative responsibilities of departments and agencies such as HMSO.

2.4 The end-user's choice of specification has an important influence on value for money. If the requirement is under-specified, the goods or services will fail to support operational objectives. Money will be wasted or further, unplanned, expenditure will be required to put things right. If the requirement is over-specified, more than necessary will be paid for the goods or services needed.

2.5 End-users are responsible for balancing performance against costs. But there are other value for money considerations in deciding on the specification. In particular, value for money can be improved by:

- maximising economies of production and supply;
- making greater use of performance specifications that encourage innovation and competition among suppliers; and
- making greater use of internationally accepted standards.

To benefit fully from these factors, there needs to be knowledge and understanding of the appropriate market and the suppliers within it. It is unreasonable to expect end-users to understand the markets with which they may have only infrequent contact. We see the responsibility for obtaining, maintaining and disseminating this information as being clearly that of the procurement organisation.

2.6 Evidence from examining officers' reports, from our discussions with the private sector and from responses to our questionnaire shows that government departments give insufficient weight to these considerations. They are thereby not getting best value for money. Two examples illustrate this:

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- the CCTA report shows that, in spite of CCTA setting up running contracts and streamlined procedures for the purchase of micro computers, over 90 per cent of departmental requirements are expressed in terms of non-standard packages. This indicates that either departments ignore the benefits from the call-off arrangement or CCTA, in setting up these arrangements, has not taken full account of departmental needs;
- a company that supplies MOD sent us details of the prices for certain goods that they quoted to MOD compared with the prices they would charge for almost identical items if MOD were to drop apparently inessential additions to the standard product. The MOD requirements added as much as 50 per cent to the price of the standard item.

2.7 To maximise economies of scale and to take advantage of available discounts, departments need to meet as many of their requirements as they can with standard or proprietary products. They also need to eliminate inessential differences between the requirements of end-users. The procurement organisation thus needs to encourage end-users to move towards common products. One private sector company told us that separate divisions of that company had for years been buying valves of an identical engineering specification but painted in different colours. By combining specifications additional discounts were secured from their supplier without affecting the product's performance. We believe that similar scope for using common specifications exists both within and between government departments.

2.8 Performance specifications tend to give better value for money than detailed specifications because suppliers can use their initiative and specialist knowledge to meet the end-user's need at minimum cost. However it may be necessary in some circumstances to supplement performance specifications with detailed specifications - for example, the quality of material to be used - to ensure the end-users' needs are met.

2.9 It is government policy, set out in Cmnd 8621,¹ that those in central government responsible for drawing up specifications should encourage reliance on standards, whether British or foreign, which hold sway in world markets. As the White Paper says:

"reducing the multiplicity of procurement specifications and relating the requirements instead to standards promotes industrial efficiency ... and increases profitability and productivity."

All of this helps to increase value for money for the purchaser.

2.10 To secure the benefits deriving from reducing inessential differences between specifications, from making greater use of performance specifications and from using international standards more fully, procurement staff must take a more active role in helping end-users to determine specifications. In MOD, the examining team found a number of instances where contracts staff had secured alterations to specifications to meet end-users' requirements at less cost. This should be encouraged in all departments and put on a formal footing. **We recommend (Recommendation 1) that procurement staff should be clearly empowered, where they can propose alternatives that they consider will provide better value for money, to challenge specifications set by end-users.** At the end of the day the end-user, or his line of command, must

¹

Standards, Quality and International Competitiveness Cmnd 8621, HMSO, 1982.

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have the final say but must reach the decision on specification in the full knowledge of the alternatives available.

2.11 We also recommend (Recommendation 2) that the senior manager in each departmental procurement organisation should set in hand a rolling review of specifications as new contracts come forward or as old contracts come up for renewal. Procurement staff should challenge any specifications that, in their view, make insufficient use of internationally accepted standards. The senior manager should set targets and a timetable for reducing the number of detailed departmental or other non-standard specifications, should promote the use of performance specifications and should monitor the organisation's achievements in these respects.

2.12 The procurement organisation's market knowledge should enable it to advise end-users on possible specification changes which would get better value for money. It should be expected to be conversant with standards (where appropriate) and should indicate to end-users the most appropriate ones for particular items. It would be required to represent the department on relevant BSI and other standards committees to present and promote the department's commercial interests.

2.13 One cautionary note: standards do not replace the need for expertise. It is necessary to understand what lies behind them. One private sector company we visited described standards as the tool of a poor engineer. While that is an oversimplification, we believe that government as a major purchaser should not simply rely on existing standards. Rather, departments should use and promote good standards to improve value for money and competitiveness. This is particularly so when existing standards are not yet internationally accepted. Government is then in the position to influence the standard to be adopted.

CHAPTER 3: METHOD OF PROCUREMENT

3.1 Once the end-user, in consultation with the purchasing organisation, has determined what is required, it is necessary to define the most appropriate method of procurement.

3.2 There are several distinct methods of procurement open to government. For example:

- purchasing low-value goods from local shops or stockists by cash or other arrangements;
- obtaining oral quotations;
- obtaining written quotations;
- inviting tenders from a range of suppliers against a formally issued specification;
- extensive formal tendering such as characterises the letting of a contract for a stretch of motorway or a major computer installation.

3.3 In each case the purchaser has to determine how many suppliers to invite to quote or to tender. The purchaser has also to determine the level (central, regional or local) at which it is best to let the contract. This level is independent of that at which goods and services are actually acquired. It may, for example, be sensible to allow a regional procurement organisation which has particular expertise to arrange and let a contract from which other regional and local units, including those from other departments, can call off supplies.

3.4 Determining the most effective method of procurement will depend on:

- what is being procured and its value;
- when and where it is required; and
- the range of suppliers capable of meeting the requirement.

All these factors need to be considered in advance if the procurement method is to maximise value for money. Responsibility for choosing the most appropriate method should lie with the procurement organisation in the light of these factors and in consultation with end-users.

3.5 We examine below, with examples from examining officers' reports, what can be done to improve value for money by adopting methods of procurement appropriate to the purchases being made.

Aggregating demand

3.6 The quality of planning in purchasing can have a major impact on value for money. For example:

- the MOD examining team considered that savings could be achieved in the government's expenditure on standard vehicles, such as cars or vans, if departments were to plan their annual requirements in

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advance and seek to reduce the spread and variety of models they purchase. If a further saving of only 1 per cent can be achieved, savings of £250,000 are in prospect;

- MOD has a central call-off contract for white loaves. They buy bread at about 6p per loaf less than the Home Office does. Between them, the two departments buy 5 million loaves a year. If the Home Office tapped the MOD contract or secured similar terms, they could reduce their expenditure on bread by 14 per cent a year.

3.7 To determine whether aggregating demand would be beneficial, purchasing organisations need to know in advance the likely requirements of end-users. Examining officers are critical of the quality of planning in government purchasing. The amount, detail and quality of information necessary to decide on the best method of procurement varies considerably. Departments do not prepare adequate plans in support of the following year's procurement budget; and there are often no useable records of the types of goods purchased in the past. If procurement organisations are to be able to decide how best to meet end-users' needs and to secure the best deal from the market, they must have this information in advance. **We therefore recommend (Recommendation 3) that the senior procurement manager in each department should draw up plans on a continuing basis, derived from past needs and forecast information from end-users, showing what goods and services are to be bought.**

3.8 Initially these plans can only be broad indications of intended purchases. Even that should help the purchasing organisation to identify areas where aggregation would be beneficial and areas where buying effort should be concentrated. Goods and services should then be divided into three broad categories:

- i. those where greatest value for money could be achieved by central contracts. Here, the position would be that the local manager could only buy elsewhere if he could demonstrate that taking advantage of a better deal would not undermine the overall benefits from a central contract (class A goods and services);
- ii. those which could be bought locally, regionally or centrally, where there might be, for example, a target price; if the local manager could obtain a better deal taking account of any additional procurement costs he should be free to buy locally (class B goods and services); and
- iii. those that can be bought at less overall cost locally, where the size of the purchase does not justify central purchasing or where local knowledge is of greatest importance (class C goods and services).

In determining how much effort to put into setting up contracts for goods and services, the procurement organisation should concentrate on class A and B goods, broadly following the 20/80 rule (that is, concentrating on the 20 per cent of goods by volume which are likely to represent 80 per cent by value). However, factors other than the volume of goods bought will influence both the categorisation of goods and decisions on where most buying effort should be put. These factors might include the need to have a high level of quality assurance or the need to support a company which has invested in order to meet a government contract.

3.9 Planning of purchasing needs to take place inter-departmentally as well as departmentally to ensure that, where appropriate, the government's purchasing power is used to maximum advantage. Smaller departments should be able to benefit from the aggregation of government orders. Aggregation of total government demand was

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the principle behind the formation of the three agencies covered by this review. But a central oversight is required to ensure that inter-departmental aggregation is pursued wherever - and only wherever - benefits can be achieved. We discuss how best to organise this central role in Chapter 7.

3.10 A further aspect of planning is the need to look at longer-term requirements. The purchasing organisation can then inform suppliers of these and, where appropriate, discuss with them how best to meet these needs. This helps suppliers to judge whether to invest to develop products to meet these needs and enables them to bring to departments' attention existing products which might meet such needs. Forward planning will also help the purchasing organisation to prepare for future work, for example, by collecting information on products for which there is to be an upsurge of demand. Procurement plans should thus include a note of identifiable major requirements and known changes in trends for future years.

Strategy

3.11 Once the procurement organisation knows what it has to buy it can plan the most effective method of procurement in consultation with end-users. Time to plan is important. Procurement which is flexible over timing is likely to produce better value for money than that which is rigid. It is ineffective to expect buying staff to set up contracts at short notice - it is expensive for government and disruptive to industry.

3.12 Examining officers' reports provide a number of examples where the choice of an inappropriate method of procurement has reduced value for money:

- an example from the report on the Home Office shows the effect of failing to recognise a product's market. The prison industries purchase a particular variety of hardwood which is produced only in the Philippines. Purchases are made from importers in the UK by standard tender procedures three times a year. The total annual cost is £783,000. Two features of the tender procedures have the effect of increasing the price paid. The first is that tender invitations are sent to several UK and EC importers, who must all refer back to the source suppliers in the Philippines to calculate their prices. This gives the source suppliers an exaggerated impression of demand; as supply is limited, the price goes up. The second is that the importer is required to quote a firm price in sterling, whereas the price he pays to the source supplier is fixed in \$US. He therefore builds an allowance into the price to cover himself for adverse trends in exchange rates. The changes recommended by the examining officer are estimated to result in savings of the order of 10 per cent of annual costs;
- the FCO report describes the new system for purchasing tyres. It used to be sufficient to know the tyre size and to go to the local stockist. Now that the tyres are purchased centrally by MOD, the NATO code has to be consulted and an Army form completed. The tyres come by National Carrier from Bicester and the bill from Liverpool. Because it all takes some time, 8 to 10 months stocks are kept in store by the FCO at Hanslope Park;
- another example comes from the ODA report. An architect on a one-year assignment to Tuvalu needed some basic draughtsman's office equipment, worth about £1,000. The architect stated that he could have obtained quotations for all the 19 items from three retail

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outlets within walking distance of his UK office. He also believed that most of the items could have been bought off the shelf in Suva (Fiji) at comparable net prices. The Crown Agents went out to formal tender. As a result it cost £2,700 (cost of equipment plus Crown Agents' charges and freight charges) to buy £1,000 of goods and ship them to Tuvalu. And by the time all the goods arrived the architect had left.

3.13 These examples show that it is important that the method of procurement is appropriate to the goods or services being acquired. The impact of all on-costs needs to be considered at an early stage in the planning of the procurement. **We therefore recommend (Recommendation 4) that the purchasing organisation and end-users agree a procurement strategy for all procurements.** For small purchases, this would normally be proposed by the end-user as part of his request for procurement action. Such a proposal would be deemed to be agreed by the procurement organisation unless specifically challenged. For larger procurements, the strategy might need to be formally discussed and agreed between the end-user and the procurement organisation. We outline the key components of such a strategy, in the context of a unified contract control document, in Annex D.

3.14 An important element in the development of any procurement strategy will be the assessment of on-costs, which must in particular take full account of the lifetime cost of the goods procured. Lifetime costings and investment appraisals are essential for all major procurements other than where the goods being bought have a very limited shelf-life. At the planning stage these analyses make an important contribution to decisions on what to acquire and the most appropriate method of acquiring it. At a later stage, they are of great value in establishing the relative ranking of individual bids, taking account of such aspects as the costs of different methods of procurement (for example supplier stocking versus departmental stocking). In this respect, these techniques can be of use even when smaller purchases are being made. The Treasury issued guidance to departments to help them conduct such appraisals in 1981.¹ This year the Treasury issued supplementary guidance which should help improve the application of this methodology.²

3.15 To obtain best value for money it may be necessary to incur higher initial costs. The longer-term implications of buying are often given insufficient weight in government because of the financial pressures imposed by a rigid annual cash budget. A recent relaxation of the annuality rules should allow departments more flexibility to take account of lifetime costing. Better procurement planning should also help. **We recommend (Recommendation 5) that lifetime costings and investment appraisals should be used to determine which products to buy. Departments should take account of value for money opportunities along with other relevant considerations in the annual public expenditure decision process and in ordering their priorities during the year. If the sums involved are significant and long-term value for money is barred by departments' annual cash restrictions, the Treasury should seek to accommodate them in the interests of securing better value for money.**

3.16 The cost of stocking what is bought needs to be given careful consideration. Call-off arrangements, particularly if they include direct delivery from supplier to end-user, can have significant advantages in reducing the overall costs of acquiring goods, even if they lead to marginally higher prices.

¹ *Investment Appraisal in the Public Sector: A technical Guide for Government Departments* HM Treasury, 1981.

² *Further guidance on the appraisal of public purchasing decisions* HM Treasury, 1984.

3.17 Excessive stocking is often a direct consequence of purchasing policy. A number of studies of stores carried out by MPO have shown that overstocking is prevalent, in terms both of the number of lines held and the numbers of items held in each line, compared to actual demand. Various studies in the private sector calculate the cost of holding stock to be about 20 per cent of its purchase price. Some studies in government departments have shown a much higher cost. The Treasury ascribe a 5 per cent opportunity cost alone to money tied up in stock. In addition, account must be taken of other overheads such as storage costs, transport and distribution costs, stock deterioration, obsolescence and loss. The MPO have issued management guidelines on stores to streamline and improve the effectiveness of storekeeping.¹ **We commend these to departments.**

3.18 To strike the best deal the procurement organisation needs to know and take account of the on-costs. It must actively keep abreast of developments in supply arrangements (such as consignment stocking). We consider that to be effective the procurement and supply (for example stores and distribution) organisations need to be in the same line management chain. **We recommend (Recommendation 6) that in formulating the roles and responsibilities of the procurement organisation (see paragraph 7.4) the Accounting Officer should include supply organisations with the aim of integrating the management structures of the two organisations if this has not already been done.** If there are sound operational reasons for brigading supply functions separately from procurement, the Accounting Officer should satisfy himself that organisational arrangements are adequate to ensure that due account is taken of all the on-costs of procurement at the planning stage.

3.19 It should be the personal responsibility of the senior manager in charge of procurement and supply to integrate purchasing and supply; to improve efficiency and effectiveness, for example by ensuring that the guidelines on stores are implemented; and to co-ordinate the activities of purchasing and supply to maximise value for money for the taxpayer.

Targeting prices

3.20 Pre-contract work should also include the setting of a target price by the end-user in consultation with the procurement organisation. Estimating a price should ensure that the buying organisation considers the underlying performance and cost assumptions of a contract. It should provide a better basis for evaluating tenders and challenging assumptions made by suppliers. Clearly the amount of work put into estimating a target price will depend on the value of the contract. Where the value is low, it may not be necessary to do more than assume the previous purchase price of the goods. Where the value is high, a great deal of work, involving analyses of raw material prices and costs of the manufacturing process, may be needed.

3.21 One private sector company we visited incorporated target prices as a formal component of their contract procedures. Targets strengthen financial control and encourage buyers to get behind suppliers' bids. **We recommend (Recommendation 7) that achievable target prices should be agreed between the procurement organisation and end-users in respect of all contracts.** The end-user should agree a target price with the purchasing organisation early in the development of the procurement strategy (see Annex D). The procurement organisation should aim to better the target price.

¹ *Stores management guidelines*, Cabinet Office (MPO), November 1983.

Suppliers

3.22 Once the method of procurement is decided, a supplier has to be selected. In choosing a supplier the aim should be to maximise the value for money obtained from the total package offered by those who bid for the contract.

3.23 Some examining officers were critical of the quality of the information held on suppliers. Existing records mainly derive from the approved lists drawn up by departments and from the outcome of tendering procedures. However, the information is not readily available; nor does it have the kind of detail which the private sector holds on its suppliers and, in some cases, its suppliers' suppliers. For example, the ODA report pointed out that:

- the Crown Agents placed more than £100,000 worth of business with 72 separate suppliers in at least one of the last three years: 22 of these obtained orders to the value of over £1 million in one or more of those years. The Crown Agents have not sought to negotiate any special terms as a result of the volume of business placed with these suppliers on the grounds that it represents very little by way of repeat orders for the same items. The German equivalent of the Crown Agents does, however, negotiate with its largest 100-150 suppliers and has achieved discounts of up to 30 per cent of the value of contracts.

3.24 The range of suppliers invited to bid for government business can also have an impact on the value for money obtained. For example, the Home Office report indicates how value for money can be increased in appropriate circumstances by inviting more suppliers to tender:

- in the Directorate of Works a special effort was mounted, through advertising and contact with trade associations, to recruit new contractors. The improved standard of competition achieved a reduction of some 8 per cent on overall prices paid by the Department.

3.25 There is evidence in some departments that new applications to go on approved lists have been rejected because departments believe that competition among suppliers already on their lists is sufficient to secure value for money. This can prevent departments from getting better deals from potentially competitive new suppliers. To overcome this **we recommend (Recommendation 8) that the senior procurement and supply manager in each department reviews all approved lists by April 1986 and subjects them to continuing review thereafter.** Firms which are not up to the mark (in terms of consistently not tendering, or having frequently missed delivery dates, or of providing goods below standard quality despite warnings) should be deleted from lists and new applicants should be added. Where possible each invitation to tender should include one firm which has not previously been invited to tender. By this means, and by always inviting a sufficient number of firms to tender, the tendering process will become more competitive.

3.26 One of the first steps in achieving good value for money is to make certain that the supplier has the capability for making goods or providing services of the required quality. Certification schemes based on BS 5750 can provide such assurance and are a central plank in the Government's National Quality Campaign. BS 5750 is a standard for the assessment of suppliers' quality management systems. It is divided into three levels of sophistication. The highest one incorporates the possibility of assessing a manufacturer's capability for designing, manufacturing and installing its products. The lowest one relates only to the inspection of final products and is

therefore applicable only to simple items. In assessing suppliers, both for inclusion in approved lists and for shortlisting for individual contracts, departments should promote the adoption of BS 5750 and, where appropriate, give due preference to suppliers who have achieved certification to an appropriate level.

3.27 Many private sector companies have close relationships with suppliers which lead to long-term and mutually beneficial arrangements. There can be advantages in establishing long-term contracts. For example, a firm may wish to make a capital investment in order to provide goods required by government at a more competitive price in the longer term. Continuity of supply may be an important consideration in placing a contract, and to ensure that may mean placing a long-term contract. In circumstances like these the procurement organisation should analyse fully the costs involved and award long-term contracts where appropriate.

3.28 It is important that the procurement organisation's management collects and analyses information on contracts placed with individual suppliers. They can then be alert to the possibility of relationships between buyers and suppliers developing to the stage where they might influence, or be seen to influence, purchasing decisions in a way that could affect the value for money obtained. It is also important that, where possible, departments discourage firms from becoming over-dependent on government business. One private sector company we spoke to spread its business so that no supplier relied on the company for more than thirty per cent of its turnover. That kind of absolute rule may not be applicable for certain specialised government procurements. But we consider that if any one department accounts for more than thirty per cent of a supplier's turnover, management should consider seeking alternative suppliers. This will avoid the possibility of being held to ransom by the supplier and the potentially difficult situation in which, by changing its needs, a department risks bankrupting a firm. It will also encourage new firms and encourage existing firms to diversify.

De-briefing

3.29 Unsuccessful tenderers will want to know why their bid failed and this information can be passed to them without breaching commercial confidentiality. Doing this helps potential suppliers improve their performance so that their future bids will be more competitive. The responsibility for de-briefing unsuccessful suppliers lies with the procurement organisation, in consultation with the end-user. The procurement organisation should take the initiative, perhaps by the inclusion of standard clauses in replies to unsuccessful tenderers.

Competitive tendering

3.30 Traditionally it has been assumed that the process of competitive tendering of itself ensures that the prices bid by potential suppliers represent the best value for money for departments. The report of the MOD examining team provides evidence that this is not axiomatically true.

3.31 In November 1983, at the suggestion of the examining team, MOD undertook an experiment in post-tender negotiation prior to the award of contracts. The existing purchasing staff telephoned the supplier who had already been selected under the existing departmental tender procedures as offering the best value for money. Their aim was to test whether, before awarding the contract and without incurring disproportionate expense to the department, further negotiation with the chosen supplier might result in improvements in the package as a whole.

3.32 The experiment did not ask staff to consider reduced specifications as a trade-off for price reductions. The ground rules suggested the use of the following tactics as a basis for negotiating price reductions with suppliers:

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- a. volume of business placed with company;
- b. any apparently undue increases from previous prices;
- c. if other than the lowest price tender had been selected because of other factors in the deal, could the successful tenderer be persuaded to equal (or better) the price of the lowest bid?

Savings of £193,000 were secured on contracts valued at over £20 million for a cost in staff time of £1,220. Price reductions achieved ranged from nil to as much as 9 per cent. Given that the experiment was conducted from scratch, that no meetings were held with suppliers, that the information base available was limited and that the buyers had little or no experience or training in negotiation techniques, the results are a tribute to the staff involved.

3.33 Further evidence that competitive tendering is no guarantee of best value for money comes from our discussions with the private sector. Nearly all the companies visited saw receiving the bids in response to a competitive tender not as the end of the purchasing process but as one stage in it. And there is evidence in the way in which foreign countries approach government purchasing which argues that a planned approach provides better value for money. For example, the ODA examining officer reported that:

- in West Germany a single procurement agency buys both for government departments and for the government's aid agency (equivalent to ODA). They have compared prices obtained for the same product at the same time on the one hand under the government procurement procedures (which do not permit negotiation on price) and on the other hand under the aid procurement procedures (which do). Prices paid under the government procedures are invariably higher, of the order of 10 per cent or more.

3.34 Post-tender negotiation provides the opportunity for the buyer and supplier to negotiate the finer points of the contract and to examine ways to reduce costs for mutual benefit. The supplier is no longer vying with competitors. As the contract is secure, subject to successful negotiation, the supplier is able to enter into frank and open discussions with the buyer and, where necessary, his suppliers and sub-contractors. As evidence of the benefits that can accrue to both purchaser and supplier from post-tender negotiation we quote from the response of one large company to our questionnaire (Annex E):

"Private sector buyers have the flexibility to negotiate an overall package of procurement with suppliers for their mutual benefit. Buyers benefit in terms of price and security of supply and service. Suppliers benefit by negotiating to optimise their manufacturing and distribution resources."

3.35 One company we visited stressed that it was just before the letting of a contract that the procurement organisation needed to put most effort into securing the best deal. This company would, for instance, seek in negotiation to secure firm commitments to spares availability and the arrangements for stocking and supplying spares. It is essential that these aspects are tied up before the contract is let. After that point, the negotiating position of the purchaser is much weaker.

3.36 If post-tender negotiation is to be successful, buying staff must be trained in negotiating skills. Some departments expressed the fear that once suppliers recognised that the successful tenderer would be subjected to post-tender negotiation they would increase their original tender prices. While this tactic is obvious we do

not believe that it will happen in practice as long as the procurement process itself maximises the benefits of the competitive nature of the market. In addition, we are not advocating that government relies on competitive tendering alone to produce good value for money but relies on skilled buyers supported by comprehensive procurement information. **We recommend (Recommendation 9) that, for individual contracts where the buying organisation considers that the benefits will justify the effort, they should introduce post-tender negotiation into their buying procedures.**

3.37 Sometimes negotiations will fail to improve the overall deal. On the basis of the information available, the procurement organisation should be able to assess if the result is reasonable or not. If the procurement organisation considers that it has still not obtained best value for money it has the option of retendering. It is possible that suppliers will resist improving their original bids knowing that departments will rarely have the time or the resources to retender. But this is equally true in private sector procurement. We believe that the key is for purchasing organisations to establish good working relationships with potential suppliers so that the post-tender negotiation becomes one in which the purchasing organisation and the supplier co-operate in reducing costs and improving the overall deal.

3.38 Our proposals above may lead to an increase in complaints from suppliers who fail to win in the competitive tender and hence do not get the opportunity to negotiate. Buyers will therefore need carefully to record decisions and any follow-up action taken, both to answer subsequent queries and for audit purposes. Departments will need to be robust in pointing out to aggrieved suppliers that they need to put in their best offer at the tendering stage. It would be inappropriate for departments to seek to negotiate with a range of tenderers after bids have been opened: that might appear to constitute a "Dutch auction" and would be damaging both to suppliers and to the credibility of government procurement.

CHAPTER 4: CONCLUDING APPROPRIATE CONTRACTUAL ARRANGEMENTS

4.1 Having selected a supplier, the next stage is to let a contract. All procurement is governed by contracts. These can be very informal such as those covering, under the umbrella of the Sale of Goods Act, the local purchase of low-value goods. Or they can be very detailed and formal, for example the contracts that cover the procurement of goods and services in support of a major construction or computer project.

4.2 On major projects, such as a computer project described in the CCTA report, careful consideration needs to be given to the implications of enforcing the contract. (In the CCTA case enforcement would have meant completely restarting a half-completed project.) Most procurement, however, is more straightforward and there is no reason not to exact contract penalties. Nonetheless, the FCO examining officer found that in a sample of contracts studied suppliers' delivery performance was particularly weak and failures to meet contract dates were rarely followed up. In DHSS, the examining officer commended one procurement branch that had recently negotiated penalty clauses in which 1 per cent of the price would be forfeited by the supplier for every working day's delay in delivery. Delivery performance had improved markedly.

4.3 The purpose of the contract is formally (and legally) to allocate responsibilities and risks between the purchaser and the supplier. The acceptance of risks or responsibilities by suppliers implies a cost or a potential cost which they will almost certainly reflect in their price. HMSO and many private companies procure many proprietary supplies under cover solely of the Sale of Goods Act. It is clear that the more straightforward the contract, the better the value for money that is likely to be obtained.

4.4 Government departments use a number of standard contracts which are of variable quality. Clarity is a contract's strength, obscurity its weakness. Securing good enforceable contracts is a specialised task. We believe that the responsibility for drawing up the contract and enforcing it should lie with the purchasing organisation.

4.5 Contracts which include scope for variation should be avoided if at all possible. However, particularly in times of world inflation, high financing costs and fluctuating demand some contracts will need to take account of variable factors. In such circumstances, the procurement organisation must take full account of, and control to the maximum extent, the impact of these variable factors in drawing up the conditions of the contract to ensure that better value for money is achieved. **We recommend (Recommendation 10) that the senior procurement manager in each department should review by April 1986 their contract documentation with the aim of making conditions more specific, clarifying risks and responsibilities and improving the form and wording.** This does not necessarily mean more complicated contracts. Indeed there is much to be said for simplifying them and relying as far as possible on the Sale of Goods Act or good quality standard contracts. Departmental Forms Units may be able to help clarify the form and wording of contracts.

Risk

4.6 One of the objectives of the purchasing procedure is to minimise the uncertainty inherent in acquiring what is needed, by when and at what cost. This level of risk varies between contracts. In a simple contract to purchase a well-tried proprietary item the risks are small. End-users are able to define clearly what is required to meet their needs; supply should be straightforward; and the contract price

is fixed. In other types of contracts, for example for computers and motorway construction, the uncertainty throughout the procurement and supply process is much greater.

4.7 These risks must be minimised if best value for money is to be obtained. Where uncertainty exists, the need for defining clear responsibilities, setting specifications, using investment appraisal techniques, targeting prices and having firm enforceable contracts increases in importance.

4.8 For example, in project work end-users need to take a much more active part in the procurement process. To minimise uncertainty they need to determine and define clearly how to meet their operational needs at least cost. The end-user will need to have the necessary expertise to set specifications and to assess the life-time costings of alternative options. In specialised areas, the end-user will need to be able to assess directly the technical competence of potential suppliers and the feasibility and costs of their project proposals. He will need therefore to acquaint himself with the specialist market, with appropriate support from the procurement organisation. The end-user will need to have a particularly close working relationship with the procurement organisation whose main responsibility will be to minimise contractual risks. In these projects, the terms of the negotiated contract will be fundamental to the achievement of value for money. Also, given that project work often spans a number of years, there is need for both the end-user and the procurement organisation to monitor contracts carefully to ensure compliance. The implications of these responsibilities in contract work are spelt out in more detail in Annex D.

CHAPTER 5: ADMINISTRATION OF PROCUREMENT

5.1 Examining officers found that many departments are unaware of the administrative costs of purchasing. Such information is progressively improving as departments introduce and refine their management information systems. Nevertheless, information is not readily available on the cost of purchasing, and this is indicative of the relatively low level of importance departments attach to purchasing. We estimate from the limited information in the departmental reports that the total cost of administering all departments' non-warlike purchasing is over £100 million a year.

5.2 Examining officers' reports identify a number of ways of improving the efficiency of procurement activities in departments. These measures will result in savings overall in the areas examined of some 10 per cent of the estimated administrative costs (see Annex B). The inefficiencies identified arise from:

- excessive paperwork;
- ineffective delegations and controls; and
- inappropriate levels of service.

We examine each of these themes in more detail below.

Excessive paperwork

5.3 Paperwork gives rise to a range of administrative costs. In particular there are the costs associated with completing, copying and moving documents to those who need the information and the costs of acting on the information once received. Individually these costs are small, but in aggregate they amount to significant sums.

5.4 At present some paperwork is inevitable. In particular departments and suppliers generally want hard copies of orders, contracts, delivery notes, invoices and payments. Modern technology is already beginning to make an impact even in these areas: for example, MOD's contractors are encouraged to accept payment by means of direct credit transfers on magnetic tape, and the Department of Transport will also be able from April 1985 to pay contractors by this means. However, most communications in the procurement process are internal signals from one part of the department to another, passing information, seeking approvals or authority for action, or accounting for expenditure. Separately, this same information may need to be stored, aggregated, manipulated and brought forward in support of procurement and management control. It is necessary to limit the information to the essential and to ensure that it is handled cost-effectively.

5.5 A number of the examining officers' reports point to the benefits that would stem from computerisation:

- the HMSO examining team commended management's efforts to introduce new technology to assist print buying staff in estimating, ordering, progress chasing, examining invoices, registering suppliers, etc. In addition, the department were employing consultants to determine a strategy for computerising other parts of their supply operation. This should result in significant staff savings over the next few years.

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- the FCO examining officer has estimated that the introduction of a micro-computer costing £20,000 in the Technical Procurement Section of Communications Division would result in staff savings of £39,000 per annum.

5.6 Computerisation offers considerable scope for doing these activities both more efficiently and more effectively. We return to this in Chapter 7.

Inappropriate delegations and controls

5.7 Financial limits on delegated authorities to individual officers vary widely between departments.

5.8 In setting levels of delegation two factors have to be borne in mind. For maximum efficiency the work should be delegated to the most junior level that can do the work effectively. But considerations of accountability will tend to reduce the level of delegation in order to ensure that decisions which have financial or operational repercussions are taken at a sufficiently high level. Getting the balance right is a matter of fine judgement. Levels of delegation cannot be determined solely in terms of financial limits. High value purchases do not necessarily imply high levels of risk; nor need they dictate a need for complex contracts. Levels must reflect the circumstances of each department, the skills and experience of their staff and the complexity of the procurement.

5.9 Staff in central government are spending the taxpayers' money. It is right that they should be held fully accountable for the exercise of this trust. This affects decisions about delegation levels because there is a perceived need to check people's work to ensure propriety. But often senior management assume that approving a certain proportion of orders provides an adequate check. On its own, it does not. Often the upshot is that the manager sees only individual cases and not the wider context of what is being done.

5.10 Most examining officers found evidence of inappropriate levels of delegation and confusion between accountability and control. For example:

- in Crown Suppliers, above a certain delegation level at least two signatures are needed for authority to issue invitations to tender to specific companies; only two cases were discovered in which the senior officer changed the range of suppliers invited to tender;
- in the FCO Communications Division, the finance section checks invoices four times before payment;
- in Transport, contractors' bills must be paid within 28 days of presentation: thereafter the department will incur interest charges. The consultant engineer certifies the amount to be paid to the contractor. This is the sum the department legally must pay. Any errors are corrected in subsequent payments. Despite this, it was found that some Regional Offices were making a series of detailed checks on technical aspects before passing the invoices to the payment section. In the payment process the information from the certificates is transcribed twice. It is a tribute to the staff that despite this system the number of late payments is negligible.

5.11 The effect of excessive double-checking is directly to increase costs and delay action. Senior staff become burdened with unnecessary work and junior staff become demotivated if they are used as post boxes and not given real responsibility.

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In all purchasing organisations it is a matter of managerial judgement as to the balance between the risk of impropriety and the cost of preventing it. In government the acceptable level of risk is generally lower than in the private sector. Effective systems of internal control need to reflect this level of risk.

5.12 Some checking is necessary. But ineffective double-checking and attention to detail at the expense of attention to major issues can become commonplace and lead to the inefficient use of staff. It is also frustrating for them. It is hardly surprising, for example, that Regional Directors of Transport should be resentful of having to seek headquarters' approval for all increases in expenditure over £50,000. The examining officer has concluded that this check adds no value.

5.13 As the Wardale Report on the PSA made clear, mechanistic checking of decision-making is ineffective. What is needed is an information and control system that assures managers that the framework of delegation and accountability is working satisfactorily and providing adequate assurance of propriety. In this context Wardale says:

"... a disproportionate amount of time and expense is incurred in operating the current systems of control, and a more cost effective approach could be adopted without any significant decrease in the levels of control. Indeed, if accompanied by more appropriate management information we believe a more effective control would be achieved."¹

5.14 Effective management control relies on a strong management structure, supported by effective management information, which requires managers to accept responsibilities. Managers' responsibilities must be clearly defined and managers have to be fully aware of the implications of their approval - for example, approving the initial financial allocation; specifying the goods; determining the terms of the contract; awarding the contract; receiving and checking the condition of the goods; and approving settlement. A typical purchase system is set out in Annex F.

5.15 Departments must decide appropriate authority levels having regard to such things as the nature of the goods being purchased; the risks involved, both financial and in not meeting the operational needs of the end-user; and the expertise of buying staff. We consider, as a guideline, that if 10 per cent or more of a person's work (by quantity, not value) needs to be referred to higher management there is a strong case for reviewing the levels of delegated authority. Current levels may be appropriate. But the evidence of this review suggests in general that the level of authority may need revision or the staff responsible for the work may be of the wrong grade. **We recommend (Recommendation 11) that the senior procurement manager in each department reviews by April 1986 the personal levels of authority delegated to staff, having regard to appropriate criteria such as those described above and to formally delegated management responsibilities.** This review should seek to retain only the minimum number of approval checks consistent with the need for propriety (paragraph 5.11). These approvals need to be recorded. We include at Annex D an example of a contract control document - based on one used in the private sector - which departments may wish to adapt for this purpose.

Levels of service

5.16 Examining officers' reports indicate that the service nature of procurement organisations has been given too little recognition. The levels of service expected of the procurement organisation are rarely made explicit. Even more rarely are the

¹ Wardale Enquiry: Final report to the Secretary of State for the Environment PSA, 1983, p43.

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levels of service related to such factors as operational urgency, cost, speed and commercial market forces. Procurement organisations have felt tied by rules and regulations which have been seen as preventing them from improving efficiency and end-users have come to accept an inappropriate level of service.

5.17 For example:

- the FCO examining officer identified 17 separate steps between the arrival of a requisition in the purchasing organisation and the despatch of an order to a supplier and as many as 24 steps if the stores section wanted to re-order stores. Partly as a result of the backlogs that had built up in the purchasing organisation, 36 per cent of the requisitions received in the purchasing organisation (51 per cent by value) were marked by end-users as needing priority action. In the examining officer's view the "priority" designation was being used to jump the queue in the procurement section rather than to alert the procurement section and the supplier to the need for prompt action to meet unexpected operational needs.
- in reporting on the difficulties experienced in procuring drawing office equipment for an architectural adviser on assignment to Tuvalu (see paragraph 3.12), the ODA examining officer commented that "as the project was handled, no-one in ODA at any time had any inkling of how long the equipment was going to take to arrive. The architectural adviser assumed that because it was basic equipment that could be bought in a shop, it would be bought and despatched with very little fuss or delay. The EO was following the rules, and again had no estimate of the timescale. The Crown Agents were not dealing with the end-user; and were unaware of his leaving date."

5.18 Procedures need to be streamlined to secure better value for money. For example, MOD's Small Value Order Cells (SVOC) manage to turn round most orders in 24 hours. The MOD team have recommended that the SVOC approach be implemented more widely throughout their department. Other examining officers have made similar recommendations designed to streamline purchasing procedures in their own departments.

5.19 End-users need to know what levels of service they can expect from the purchasing organisation. All too often line managers accept a poor level of service because of ill-defined responsibilities. In particular it is necessary to define what the procurement organisation requires from end-users, and by when, if it is to make an effective purchase. Within these constraints the procurement organisation should undertake that the agreed specification, target delivery date and target price will be met; that it will seek to improve the target price; and that it will satisfy the information requirements of the end-user. **We recommend (Recommendation 12) that the senior procurement manager agrees in writing with end-users by April 1986 service agreements defining the levels of service which the procurement organisation will provide.** He or she should be responsible for the performance of the purchasing organisation as measured against the service agreements.

5.20 To draw up these service agreements, all government departments will have to review the management structure and responsibilities of their present procurement organisations to determine whether the needs of end-users are being met. Service agreements will provide a framework for the operational responsibilities between the purchasing organisation and end-users. They will need to reflect the different types of procurement that can be undertaken. They may be specific to individual end-users or they may be department-wide.

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Management information

5.21 The key to assessing whether the terms of the service agreements are being met is the right information being available to the procurement organisation. This must enable managers to measure and control the effectiveness of the purchasing organisation and the performance of the staff in it. They should, for example, be able to derive statistics on:

- the number of orders placed;
- the type of product or service purchased;
- the price paid compared with the target price;
- suppliers used; and
- delivery and quality performance.

Ratios can be developed from these statistics to provide management with performance information on the organisation. Appropriate measures might be the cost of the procurement organisation in relation to the throughput of orders (by number and value); the ratio between orders placed and late deliveries; performance as against the terms of the service agreement; stock ratios; actual prices as compared with target prices; etc. The information should also enable management to check on the progress of particular orders and to identify where problems have arisen or are likely to arise.

5.22 We have made a number of recommendations designed to give purchasing staff greater flexibility and responsibility. This needs to be matched, as noted in paragraphs 5.7 - 5.15 above, by monitoring and control systems that provide for effective management. The management information system must both deter and assist in the detection of any potential impropriety.

5.23 **We recommend (Recommendation 13) that the senior procurement manager and his senior line management agree the basis of, and firm plans for developing, appropriate management controls for procurement, by April 1986.** Some of the required information may be available from existing financial management systems. But it will need to be extended and to be available on a timely basis to support day-to-day management.

5.24 The management and procurement information systems (see paragraphs 3.7 and 3.25) will share a common database - the only differences between the systems will be the purposes for which information is extracted. The management information system, as well as supporting immediate line management, will need to underpin the budgetary and review functions of departmental top management systems being developed in the context of the FMI.

CHAPTER 6: MOTIVATION

6.1 Getting better value for money in government procurement depends on the staff involved. We compared the way in which the private sector and government manage the purchasing function. Private sector companies regard their purchasing department as an integral part of their operations. Their profitability depends on getting value for money for what they buy, whether it be goods for resale in a retail chain, the components needed for a manufacturing process or the goods and services making up a major construction project.

6.2 Four main themes ran through our discussions with private companies:

- buying is a career where people develop expertise in negotiation, markets and products over a number of years. In some areas the specialism encompasses the whole of the supply process and in others buying and selling are seen as part of the same career structure;
- identifying the right people for buying is important. Once picked, they need thorough training if they are to be fully effective;
- buying staff are set high but achievable performance targets. There are financial rewards for reaching these targets; and
- the buying department has a high status in the organisation. Staff are well motivated to perform effectively.

The private sector regards these factors as important in obtaining effective and efficient performance from their purchasing departments. We believe that in government buying these factors should be given similar prominence.

6.3 At present only a few departments treat buying as a specialism. In most, it is often just another posting. The training given is mainly on-the-job and, except in a few areas, performance targets are not set. In general, buying is not regarded as a high status job and, in consequence, the staff are not as highly motivated as they could be. Our report advocates increased and clearer responsibilities to help improve both status and motivation. Purchasing staff will see that their job is important and that senior management regard it as a valuable part of the department's work. But more needs to be done and it needs to be done urgently.

6.4 To effect change quickly, and to keep up to date with the best private sector practice, we consider it essential that departmental procurement staff have relevant private sector experience. Arrangements for the interchange of civil servants with industry and commerce already exist. **We therefore recommend (Recommendation 14) that the senior procurement manager in each department sets up a specific programme within these arrangements to recruit or second buying staff from the private sector, and a specific programme of secondments to the private sector, by no later than April 1986.** The need for this experience is particularly important at senior levels in the purchasing and supply organisation.

6.5 A first step to attract and retain the right people in buying is to identify staff with a talent for the job. Senior procurement managers should be required to set out for establishment divisions the qualities needed by staff involved in purchasing, drawing as necessary on private sector experience. We also believe that government should recognise buying as a specialism and structure the purchasing and supply activities of departments to promote career development. Initially this may

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involve keeping people in purchasing and supply organisations for longer than is currently usual in most departments. The aim should be to reach the position where staff in government purchasing organisations regard themselves as buyers rather than as generalist civil servants.

6.6 However, few departments have procurement organisations large enough to provide a career path for buyers. And there is a need to associate buying and supply closely so that people pursuing such a career gain experience and training in the whole procurement process. We therefore believe that, in the longer term, career paths will need to be across departments, as occurs in other functional specialisms. There are a range of possible patterns, from an arrangement akin to those for government accountants to the creation of a separate professional group. **We recommend (Recommendation 15) that the Cabinet Office (MPO) in consultation with departments develops a functional specialism for purchasing and supply**, drawing as appropriate on experience within the private sector and within departments with a large purchasing organization such as the agencies or MOD. Specialisation should help to encourage greater movement in buying personnel between departments and the private sector. Greater co-ordination of career management should assist small departments for whom the full-scale implementation of our recommendations on secondments and training may be difficult to achieve in isolation.

6.7 Next, there is a need to provide training in basic buying skills and to provide courses to develop buying techniques and negotiation skills. Some private sector companies we visited sent their staff on courses run by the Institute of Purchasing and Supply (IPS) and some staff sit the IPS examinations. Others ran their own training in-house. No-one relied solely on on-the-job training. **We recommend (Recommendation 16) that the senior procurement manager in each department devises and initiates a training programme for staff involved in procurement by April 1986.** These programmes should be developed by departments' training divisions after consulting the staff involved and with the help of the Civil Service College and outside consultants as appropriate.

6.8 There is also a need to measure the performance of staff to determine whether better value for money is being obtained. Performance criteria need to take account of such things as price, quality and delivery time. The management information systems developed by departments must be designed to identify these and other key statistics (see paragraph 5.21). In the private sector a variety of performance measures are used. In one company we visited prices were the main criterion, with individual buyers being given targets related to inflation, the prices achieved by other companies in the group and the historical prices paid for the goods in question. In others, a global performance assessment was used, taking account of not only price but also level of service to end-users. Buying staff have to be involved in the process of determining such performance criteria.

6.9 We do not think that it is possible to lay down criteria which would apply in every department. In some areas, such as MOD's small value order cells, the major criterion may well be speed of service. In such an organisation a performance target related to the length of time taken to place an order might be most appropriate. Organisations may wish to place equal importance on quality and to assess performance on rejection rates. **We recommend (Recommendation 17) that the senior procurement manager, in consultation with the staff, draws up performance targets for individuals or groups of individuals by April 1986,** based on appropriate levels of service and on prices.

6.10 The performance of staff against these targets will be a measure of their achievements and, as such, will act as a strong motivator. However, we believe that, given the important role of buying staff in improving value for taxpayer's money, all

available means need to be used to stimulate high performance. We conclude that direct financial rewards for exceptional performance would be a useful addition to the other proposals we make. The nature of the reward may have to await the outcome of more general decisions on Civil Service merit pay. However, we believe that for buyers and, where appropriate, their supporting staff a scheme of non-pensionable bonuses would be appropriate. The schemes should be introduced on an experimental basis and the staff involved should be consulted on them. **We therefore recommend (Recommendation 18) that by April 1987 departments introduce incentive schemes for buying staff, based on performance targets and taking account of decisions on Civil Service merit pay generally.** Coupled with such schemes needs to be an acceptance that staff who find that they are unable to meet performance targets should be allowed to move to other work as soon as possible.

6.11 Another form of motivation is pressure from the end-user to provide a certain level of service. We consider this pressure is necessary to balance the cost of procurement against the value added by the buying staff. One company we visited operated a centralised buying section where end-users were charged a standard fee for each order placed. The buying organisation was required fully to recover its costs. This forced end-users to take account of the cost of the buying section's services and to challenge those costs. In turn, this put pressure on the buying organisation to improve efficiency, reduce costs and provide good value for money to end-users.

6.12 The costs of the purchasing organisation could be recovered by periodic transfers from the budgets of end-users, or by a percentage add-on to the price of the goods and services. Such repayment schemes need to take full account of the relationship between the end-user and the buying organisation, the amount being purchased and the effort put into the purchase by the buying organisation. We believe that in major procurement areas recognition of procurement costs by repayment would be beneficial. An internal repayment system needs to be carefully devised if the benefits are to outweigh the costs. Thus, while we think such a system should be introduced, we suggest that further work on the practical aspects needs to be undertaken. This would fall to those responsible for following up progress in implementing our report.

CHAPTER 7: MAKING THINGS HAPPEN

7.1 Our report shows that, overall, government procurement costs the taxpayer too much. Administration costs are too high; and the prices paid are often higher than necessary. What finally convinced us that government buying could be improved was a comparison with the private sector's approach to purchasing. While we are not able to comment on the absolute quality of private sector buying, we believe buying sections in the best of private sector companies are more active, better informed and better motivated than in government. There is a drive and energy that is uncommon in government purchasing organisations. Also there is an appreciation of the importance of the purchasing function which is largely absent at senior levels in government departments.

7.2 Purchasing is an important activity in government. It consumes about £14,900 million of government resources. It has to be effective if operational needs are to be met. Our report identifies a number of things that are wrong and recommends ways in which they can be put right. We conclude, however, that progress can only be achieved if the right management framework for making the changes exists.

7.3 We believe three important steps need to be taken:

- roles and responsibilities need to be clearly defined;
- a single individual in each department needs to take personal responsibility for making the changes happen; and
- a central focus for procurement practice throughout government needs to be established.

Roles and responsibilities

7.4 We believe there is a need first and foremost to ensure that end-users and procurement organisations understand their roles and responsibilities. Our report will help in this. But these roles need also to be formally prescribed and promulgated by departments to all concerned. **We therefore recommend (Recommendation 19) that the Accounting Officer, together with the senior manager responsible for procurement in each department, develops a formal statement of the roles and responsibilities of the departmental procurement organisation and ensures that this statement is communicated to all staff both in the procurement organisation and in spending divisions by October 1985.**

7.5 Throughout our report we have identified the main responsibilities of the purchasing organisation and the end-user. Annex G lists these.

Director of procurement and supply

7.6 There is a need for an individual to take personal responsibility for making the changes happen. **We recommend (Recommendation 20) that the Accounting Officer of each department appoint or designate a director of procurement and supply to take on these responsibilities.** This should happen before July 1985. The grade of the person appointed will depend on the level and complexity of purchasing in each department.

7.7 The director's operational aim will be to meet the needs of end-users and secure improvements in value for money. His or her main priority will be to make

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progress in improving the efficiency and effectiveness of the procurement organisation. We have set target dates for making the necessary changes. The director will be required to report progress on implementation on a regular basis to senior line management and centrally.

7.8 Other tasks for the departmental director arise from our earlier recommendations on the roles and responsibilities of the procurement organisation (listed in Annex G). The list is not exhaustive. The nature and amount of goods and services bought differs from department to department. In the light of these variations, directors will have to define the details of their own jobs and they should have the discretion to do so within the framework of the formal statement recommended in paragraph 7.4.

7.9 In recognition of the vital contribution of good buying to profitability, the private sector's approach to purchasing has developed a great deal over the last 10 to 15 years. It is crucial that senior purchasing staff in government departments have comparable skills and experience in order to deal with the private sector on equal terms. We therefore consider it desirable that the director of procurement and supply should have recent commercial experience in buying.

Central co-ordination

7.10 At present, the main focus for procurement in the central departments is AP Division in the Treasury. It is responsible primarily for procurement policy, though it issues some practical advice on such matters as investment appraisal.¹ In addition, the Department of Trade and Industry is responsible for promoting the Public Purchasing Initiative. It is clear from the evidence in our report, however, that a central focus wholly devoted to procurement practice is needed. Such a central reference point is necessary in order to gain the full benefits from our recommendations, to change the culture of government buying and to provide the necessary support to departmental directors of procurement and supply.

7.11 **We therefore recommend (Recommendation 21) that the Prime Minister approves the establishment of a small central purchasing unit (CPU).** This should be in business by January 1985. The CPU should be set up initially for a period of three years, after which the need for its continuing existence should be reviewed. The unit's objective would be to develop and secure increased effectiveness in purchasing and supply throughout central government within this three-year period.

7.12 To achieve this it will need to encourage and monitor progress based on the action documents departments will produce in response to our recommendations. The progress reports of departmental directors of procurement and supply should be submitted to the CPU for incorporation into a central progress report to the Prime Minister (see paragraph 7.25).

7.13 Another key task of the unit would be to provide advice on good buying practice to departments. It will also need to co-ordinate inter-departmental aggregation, nominating lead buying departments as appropriate. These, and the other tasks for the unit which derive from our recommendations, are listed in Annex H.

¹ *Investment Appraisal in the Public Sector: A technical Guide for Government Departments* HM Treasury, 1981.
Further guidance on the appraisal of public purchasing decisions HM Treasury, 1984.

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7.14 The Central Purchasing Unit should consist of no more than five people with staff support. Its head should have direct access to ministers. As we stress throughout this report, buying is a speciality. Thus the CPU, to be credible, must contain proven practical expertise. The head and two other members of the unit should be seconded from the private sector, one experienced in contracts work. We have not been able to recommend where the unit should sit but in Annex H we consider a number of possibilities.

7.15 Consistent with the principles of the FMI, the unit should not detract from the independence of departments to buy what they want at the price they wish to pay. What it can do is help departments obtain better value for money in purchasing.

7.16 We estimate that the CPU's running costs, including salaries, support services and accommodation, will be around £300,000 a year. This is a small sum when set against the contribution the CPU can make to achieving the savings targets.

Targets for savings

7.17 The implementation of our proposals for streamlining the procurement procedures, for reducing the size of stocks being acquired by departments and for obtaining better value for money in purchasing should achieve large savings. This is backed by the findings of individual examining officers. All of them pointed to scope for reductions both in the administrative costs of purchasing and in the prices paid for goods and services. Most set short-term targets for savings in their departments.

7.18 Many private sector companies set target reductions as a means of initiating progress. Once improvements are seen to be happening, the targets are refined so that the initial progress is consolidated and further improvements obtained. Using this approach private sector companies have considerably reduced their total purchasing costs in recent years. We believe that this approach should be adopted by departments.

7.19 Setting targets for savings in the procurement area is not straightforward. On administration costs it should be simple to demonstrate whether the streamlining we recommend has led to a reduction. Taking examining officers' reports as a whole, their recommendations for reducing administrative costs amount to around 10 per cent of current costs. Applied to all non-warlike purchasing we estimate that this would save over £10 million a year and we believe that this is achievable by March 1987.

7.20 Setting targets for reduced storage and distribution costs is more difficult, not least because many departments are unable to place a reliable valuation on the stocks they hold. Stockholding and distribution costs will be reduced by the greater use of call-off contracts. This, combined with the implementation by departments of the Cabinet Office (MPO) guidelines on stores,¹ should produce substantial savings. Government's non-warlike stockholdings are broadly estimated at £5,000 million. If these can be reduced by 2 per cent, a once-for-all saving of about £100 million is possible. In addition, this would attract annual savings of around £5 million mainly from reduced accommodation and staffing needs. A further, more detailed paper on this is being prepared by the Cabinet Office (MPO) and will be made available to departments to apply appropriate lessons to their own procedures and holdings.

7.21 We believe that, as a result of our recommendations on aggregation, specification, supplier development and competitive tendering, government

¹ *Stores management guidelines*, Cabinet Office (MPO), November 1983.

departments can obtain better prices for the goods and services they buy. This is confirmed by the private sector, who have made similar improvements, and by examining officers' findings. Estimating how much by way of savings that will yield is difficult. First, the quantity of goods and services bought each year will vary. Second, specifications may change. Third, needs may change, for example, the Department of Transport may at some time choose to spend more on road maintenance and less on new highways.

7.22 It will also be difficult to measure how much keener are the prices achieved and whether they are achieved by the efforts of departments or by other factors. It is a hypothetical question as to what would have been the unit cost of a good if a more enlightened procurement practice had not been adopted. And, there may be some areas, such as information technology, where improvements in the design and manufacture of the goods could lead to price reductions without any effort on the part of a procurement organisation.

7.23 We believe that it is unrealistic to allot a single target on prices to everything bought by every department; or, indeed, to set the same price reduction target for each department. There are some industries where supply currently exceeds demand (for example construction and clothing). If that changes, getting any improvement in prices will be extremely difficult. The examining officers' reports show that departmental performance on prices varies greatly. For example, there is no doubt that the three agencies covered by the review obtain excellent prices for those goods they buy in bulk. Similarly MOD have probably obtained very good deals on some of their large orders, such as that for bread (see paragraph 3.6).

7.24 The evidence from departmental reports indicates that, broadly, a 5 per cent reduction in prices can be readily achieved by adopting some of the approaches we describe above. We believe that the strategy we outline will lead to savings in excess of this. The extent of the overall reduction lies anywhere between 5 per cent and 20 per cent of the amount spent on non-warlike goods and services. If it was 5 per cent the saving would be nearly £400 million, and if 20 per cent, over £1,500 million.

7.25 Targets must be set to secure savings in administration costs, storage costs and prices. The approach we propose is that departmental directors of procurement and supply should draw up such targets. For goods and services the target should stem from the departmental procurement plan and should be based on the unit costs of major items to be bought. For projects, criteria for success for specific procurements will have to be drawn up. **We recommend (Recommendation 22) that departments should draw up such targets and criteria for submission to, and agreement with, the CPU by April 1986.** The targets and criteria should be supplemented with a timetable showing when cost reductions are progressively to be achieved. They should identify separately the savings to be achieved by better administration, reduced on-costs (storage and distribution) and better prices.

7.26 Once the targets have been agreed with the CPU, in consultation with the Treasury, it will be necessary to monitor performance against them. Achieving the targets will only be possible if departments act to improve their purchasing organisations. The CPU should monitor these improvements. Expenditure divisions in the Treasury will be able to monitor achievement against the targets by assessment of departmental expenditure bids, in consultation with the CPU. As part of the monitoring function of the CPU, **we recommend (Recommendation 23) that the unit report to the Prime Minister by June 1986 on the steps taken by departments to set up the organisation to achieve savings; and by June 1987 further report to the Prime Minister on the success of departments in achieving their savings targets.**

The costs of implementation

7.27 The recommendations for change made in our report are designed to improve the whole approach to government purchasing. To make purchasing more business-like will involve an investment both in the staff concerned and the systems needed to support them. Some departments have already established training schemes and are introducing computerisation into their purchasing organisations.

7.28 A particular problem could arise from the level of manpower required for purchasing. Some departments, particularly those identified as lead departments for aggregated purchases, may require additional manpower, though this would be offset by staff savings in other departments. There may be a need for limited additional resources to get the process of change under way. However, most of the examining officers have identified areas where staff reductions can be made, and we believe that other departments should be able to find similar economies. Part or all of these savings may need to be reinvested in more cost-effective procurement activities. If departments conclude that additional staff are needed to obtain better value for money, they should give priority to such demands in the context of the overall savings, both financial and manpower, to be achieved through implementation of our recommendations, and within government policy on manpower numbers.

7.29 A number of our recommendations are designed to improve the information available to buyers and their managers and to streamline the procurement process. Computers will have an important part to play in this, in particular:

- for procurement information databases;
- for management information databases;
- for information on suppliers;
- for internal communications (eg cataloguing, progress chasing), order processing and word processing (eg standard contracts).

7.30 The development and maintenance of these systems will require further investment. Each application will need to be considered separately and decisions taken on the basis of sound cost-benefit and investment appraisal analyses. In the private sector such investment has been shown to be necessary and worthwhile. The evidence of this review indicates that government should follow their example. **We recommend (Recommendation 24) that the director of procurement and supply in each department develops a strategy and has firm plans for the development of the necessary information, monitoring and control systems set out above by April 1986.** This will be a major task for most departments, requiring careful planning and a high degree of expertise.

7.31 The form and complexity of the information systems should have regard to the information needs of buyers and their managers. The systems will also need to have regard to other departments' systems. Compatibility between departments should help to ensure that government has the necessary information to plan central contracts and receives the full benefits of aggregation.

7.32 We believe that each of the changes we recommend would on their own lead to some improvement. But we have designed our proposals as a package to ensure the maximum improvement in value for money for the taxpayer. Only implementation of the whole package will secure anything like the savings we consider achievable.

CHAPTER 8: AGENCIES

8.1 Around 12 per cent (£1,700 million) of all central government departments' expenditure on goods and services is spent through the central agencies. Their performance, in terms of both efficiency and effectiveness, will thus have an important part to play if departments are to achieve their savings targets. This chapter deals specifically with the three agencies that took part in the review. (A general note on them is at Annex I). We make a number of recommendations to improve their effectiveness. What we say will have application to parts of the other agencies - for example the building maintenance divisions of PSA. Departments that sponsor the other agencies should consider the extent to which our recommendations are relevant to them.

8.2 The primary role of the three agencies is to arrange the purchase and supply of common goods and services to departments. The agencies define their operating objective as being to ensure that departments and government as a whole receive best value for money. Centralised procurement and supply helps to achieve this by taking advantage of:

- lower prices through aggregating requirements;
- high technical and buying expertise;
- efficient storage and distribution arrangements;
- lower administrative costs.

8.3 There is evidence that the three agencies get keen prices. In a study undertaken by the Ministry of Defence covering ten product areas, the products supplied by HMSO in nine of these cost less than quotes from alternative suppliers. And a number of price indicators devised by the Treasury and the agencies all show that average prices charged by the agencies are competitive.

8.4 The three reports reveal that the agencies have all gone some way to improve their buying organisations. Much of the improvement is along the lines described earlier in our report. For example, in HMSO print procurement the buyers have detailed knowledge of their potential suppliers' workload and are able to match jobs to suppliers' capacity with advantage both to the supplier and the department. CCTA have introduced personal levels of financial delegation. Crown Suppliers have commissioned a number of reviews which when implemented will improve their procurement and management information systems.

8.5 The review did not specifically cover the question of stores and distribution. However, Crown Suppliers have their own storage and distribution network and HMSO their own storage system. However, CCTA arrange all their contracts so that there is direct delivery from suppliers; and 65 per cent by value of Crown Suppliers' contracts and over 80 per cent by value of HMSO's are on a similar basis.

8.6 The review did not extend to consideration of whether overall administration costs are minimised through the use of central agencies. However, all three examining officers identified ways in which the efficiency of the purchasing organisations could be improved. These, together with our recommendations earlier in this report, should further increase the efficiency of the agencies.

Effectiveness of the agencies

8.7 Central purchasing adds an extra link to the chain of supply as departments do not deal directly with suppliers. The extra link may add cost and delay to the process.

8.8 Departments are tied to both Crown Suppliers and CCTA, that is they are expected to buy the goods and services provided by the agencies from them or on contracts arranged by them. In the case of HMSO, there was formal untying in 1982, though HMSO then negotiated customer agreements with all but one department. These agreements are seen by departments as tying in all but name. However, even the exception, DOE, buys over 90 per cent of its stationery requirements from HMSO. In addition, both HMSO and Crown Suppliers do substantial business with public sector bodies not tied to them whether formally or through customer agreements. This evidence suggests that the combination of price charged and quality of service delivered by the agencies is good.

8.9 However, there is evidence in the HMSO report that the benefits of centralised purchasing are being to some extent dissipated. This is because HMSO will provide whatever is required in whatever quantity to departments. The administrative costs of processing small quantities or non-standard items are not wholly charged to departments. Instead they are spread over all the goods and services provided so that the high value, high volume commodities subsidise the administrative costs of small purchases.

8.10 This approach is also taken by the other two agencies. The examining officer in Crown Suppliers recommended that the level of departmental expenses (in essence the administrative costs passed on to departments) should be further refined in order better to reflect the true costs of supply. CCTA charge a single rate of 2½ per cent on all purchases up to £1 million and 1 per cent thereafter. The CCTA report recommends that a more logical basis of charging should be adopted to reflect the resources expended on different types of procurement.

8.11 We believe that the strength of the agencies lies not in providing a comprehensive service but in concentrating on those goods and services which are required in high volume by departments and on those goods and services where either the product (for example computers) or the procurement (for example printing) requires a high level of expertise best concentrated at the centre. The pricing structure should be refined to reflect this so that standard goods are available at very competitive prices and the price of non-standard goods reflects the full cost of purchasing and delivering them. Thus the strategy of the agencies should be based on their ability to make full use of economies of scale and the need to have a product range which will attract sufficient customers and sales to minimise on-costs. **We thus recommend (Recommendation 25) that the three agencies review fully both the range of products they supply and their price structures to enable them to meet this overall strategy.** The price structure could well include setting a price level for low volume non-standard goods at such a level as to discourage departments from buying such items from the agencies.

8.12 Departments need to plan their purchasing so as to enable the agencies to determine where and how they can best meet departmental requirements. The departmental procurement plans (recommended in paragraph 3.7) and the work of the CPU will provide the information needed to identify which goods are best bought under a central arrangement. Where appropriate such contracts would be arranged by the agencies. These plans should be backed up by consultation between departments and the agencies to identify those goods and services to be provided under central contracts.

8.13 In line with the categorisation described in paragraph 3.8 there are some goods and services which it makes sense for all departments to purchase through an agency unless they can demonstrate an economic case for not doing so (Class A). There are others for which a central contract is useful but need not prohibit departments buying elsewhere if a good deal is available (Class B). Having identified these, and the likely volume to be required, the agency will be required to negotiate the best possible contracts for each of the goods and services. However, in order to get best value for money it will be necessary for the agency to have some assurance of the degree of business to be conducted under a central contract. Thus departments will have to enter into some commitment to the contract. The nature of that commitment will vary depending on whether or not Class A or Class B goods and services are being bought.

8.14 We do not propose that the commitment be expressed in the form of customer agreements which are comprehensive and open-ended such as those that currently exist between HMSO and departments. Instead **we recommend (Recommendation 26) that the procurement organisations in departments set up supply and service agreements with the agencies by March 1987 to formalise their operational relationships.** These supply agreements will reflect the contracts which agencies arrange in terms of price, service and product specification. They will provide departments with a clear set of criteria against which to judge whether an alternative source of supply would be more cost-effective, even with the additional costs the department will incur in going it alone. For Class A goods and services, not signing the supply agreement would require justification on economic grounds.

8.15 Having committed itself by signing a supply agreement, a department will be able to withdraw:

- if it can demonstrate to the CPU that an alternative deal would be in the general interest (ie for Class A goods and services an economic case must be made before withdrawal); or
- if, in the case of class B goods, it can get a better deal elsewhere, merely reporting the fact to the CPU and agency; or
- if it can demonstrate to the CPU that its operational needs have changed such that the original contract can no longer satisfy them; and
- if it gives sufficient notice to the agency to allow it to attempt to renegotiate a better deal. (We suggest the notice should only be more than six months if the agency can demonstrate to the CPU that it will take longer than that to amend the contract.)

8.16 To determine whether or not an alternative supplier to an agency provides a better overall deal, departments need to know the total costs of purchasing, including their own administrative costs. Our earlier recommendations should ensure that increasingly they do. It is implicit in our proposals above that departments must have the freedom to use alternatives where justified. Thus, **we recommend (Recommendation 27) that departments are formally untied from Crown Suppliers and CCTA by April 1987.** This will have the additional benefit of providing the agencies with yet a further spur to improve their competitiveness.

8.17 In addition to providing the means of access to goods and services, the agencies also provide some goods and services directly to departments. For example, HMSO provides a forms storage and distribution service for departments, CCTA provide technical advice and Crown Suppliers provide a design and a car service. The review did not cover these activities.

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8.18 However, in our discussions with the private sector we noted that they took a different approach. For example, one large organisation did not directly involve itself in storage and distribution which was carried out for them by a company which specialises in it. Similarly another company needed to test paint; it took the view that that was not part of its business and contracted out the testing to a specialised organisation. We also note that, from April 1982, the distribution of goods from Crown Suppliers' stores has been contracted out.

8.19 There may well be scope for the agencies to adopt this approach more widely. There may be cases where the "in-house" service provided by the agencies delivers better value for money than contracting out would. Or it may be essential for operational needs to provide the service "in-house". We were, nonetheless, concerned that Crown Suppliers and HMSO felt it necessary to have large stores, though HMSO have recently effected a major reorganisation of theirs. We were also concerned that certain businesses carried on by the agencies could equally be provided by the private sector - for example, the car service provided by Crown Suppliers. We see the direct provision of these services as potentially detracting from the main objective of providing access to goods and services. Therefore **we recommend (Recommendation 28) that the three agencies collate such information as is already available on the relative cost-effectiveness of those activities not directly concerned in achieving this main objective; supplement it with such other information as is necessary; and present it to ministers in their sponsoring departments with recommendations on the feasibility of contracting out by March 1986.**

8.20 The examining officers in HMSO and Crown Suppliers considered whether the effectiveness of the agencies would be improved by a merger. Their conclusion was that the theoretical advantages - particularly in terms of developing a cadre of professional buyers - would be outweighed by the practical problems. We agree insofar as the agencies continue to carry out the diverse range of activities which they currently undertake.

8.21 However, the changes outlined above would mean that the agencies were mainly in the business of arranging contracts for goods and services which are common to all departments. Rationalisation on these lines may reduce the practical problems in achieving merger. This should be borne in mind by the heads of the agencies in implementing our recommendations. They, the head of the CPU and the central departments should review the scope for reducing the number of agencies once the new strategy outlined in this chapter is operating.

CHAPTER 9: GOVERNMENT POLICIES ON PROCUREMENT

9.1 This chapter considers four aspects of government policy which affect buying by departments:

- the Public Purchasing Initiative (PPI)
- small firms policy
- preferred suppliers
- EC and GATT rules

The Public Purchasing Initiative (PPI)

9.2 The guidelines for the PPI were promulgated by the Treasury in March 1981 and are reproduced at Annex C. Essentially, the policy is one of enlightened self-interest. It encourages departments to develop relationships with suppliers which will ensure that value for money is obtained by government and stimulate industrial competitiveness and innovation. The aims of the PPI are entirely consistent with the approach we have advocated in this report.

9.3 Examining officers found that the implementation of the PPI is, at best, patchy. In some departments, such as HMSO, a positive effort has been made to operate the policy and to interpret it to buying staff. In contrast, in some other departments implementation has consisted largely of circulating the Treasury guidelines. The guidelines are an excellent statement of philosophy, but they are not a comprehensive guide to action.

9.4 The recommendations which we make in earlier chapters are intended to improve the skills and expertise of buying staff to enable them to get better value for money in purchasing. They provide a framework for good practice in buying in much the same way as the PPI set out to do. It seems that up to now the PPI has been often regarded as something extra to be tagged onto the buying process rather than an integral part of it.

9.5 We consider it to be an important function of the proposed CPU to give guidance on good practice. This would incorporate the Treasury guidelines, but develop them as practical advice to buyers. It should also provide advice on the appropriate use of British and international standards and on the use of quality assurance standards. We envisage this guidance covering all aspects of the purchasing and supply process. It would need to be incorporated fully into departmental purchasing manuals. It should also serve as a basis for audit of purchasing and supply functions. **We recommend (Recommendation 29) that the CPU, in consultation with Treasury and DTI, prepare such guidance by April 1986.**

Small firms policy

9.6 It is government policy to encourage the development of small firms. One way of doing this is by improving access to government business. We do not interpret this as favouring small firms irrespective of their competitiveness.

9.7 Government does not hold central records of how much of its business is awarded to small firms. But there is evidence to suggest that a substantial amount of government purchases are supplied by this sector. For example, the examining officer in the Home Office found that 68 per cent of a small sample of suppliers employed fewer than 100 staff.

9.8 Some progress has been made in improving accessibility to government contracts. For example, the Treasury has recently reached agreement with departments on a standard form of factual enquiry, covering financial and general information, to be sent to potential new suppliers. Previously each department sought its own information with the result that a firm might receive a large number of questionnaires from different departments all seeking much the same information. The Minister for Small Firms announced in November 1982 that firms would no longer need to have approved status for the award of most government supplies contracts under £2,000 (now £10,000); that non-approved firms could bid for non-urgent supplies contracts above this level subject to their approval subsequently if successful; and that there would be a greater rotation of invitations to tender amongst firms on departments' lists. In addition, DTI has produced a booklet aimed at helping small firms to understand the procedures they may have to go through in order to get government business. The booklet gives a brief account of what departments buy and lists contact points. Some individual departments - MOD, PSA and HMSO - have produced more detailed booklets on their own purchasing procedures and requirements.

9.9 Small firms need to know what goods and services government buys now and may want to buy in the future. We were impressed by the efforts of one large private sector company to ensure that local firms in the areas in which they operated were aware of the opportunities available. This was done through production of a simple readable guide to the kind of goods the company purchased and how to get on its approved list. Some comparable booklet is needed to introduce government business to firms of all sizes. This need include no more than a list of the main goods and services bought by government together with which departments buy what, a list of contacts in departments and a copy of the factual questionnaire mentioned above. The booklet *Tendering for Government Contracts*, prepared by the Department of Industry and the Central Office of Information in 1981, meets this need in part. We consider that it should be expanded and regularly updated. The information required for this could be readily derived from departmental procurement plans. Since these procurement plans will be coming to CPU, the Unit should be consulted by DTI when they are preparing revisions of the booklet. Steps should be taken by DTI actively to promote the booklet throughout the small firms sector. This should help small firms to identify opportunities for government business. It may need to be supplemented by more detailed information distributed by individual departments.

9.10 At present a company wishing to sell the same goods to different departments generally needs to satisfy each department separately as to their fitness to be included as a potential supplier. As far as possible, approval by a department should represent approval by government. We see a role for the CPU in reducing paperwork both for the supplier and government by encouraging the use of inter-departmental approved lists and simpler, standardised procedures affecting small firms. This stresses the need for a co-ordinated approach to information systems.

9.11 Encouraging small firms to bid for government business will involve a small cost to departments. But even if only a small proportion of the new firms which apply to be added to approved lists are successful in securing a contract, the longer term savings to departments should outweigh the costs.

Preferred suppliers

9.12 Sheltered workshops for handicapped people and prison workshops are designated priority suppliers. They are shown preference in the award of contracts and are given more favourable opportunities of supplying the widest possible range of goods. In brief, the system provides for priority suppliers to be awarded a proportion of contracts they have been unable to secure competitively. A similar preference is

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given to firms in development areas. In neither case does this extend to a price preference. We do not question the validity of these policies. In both cases preference is subject to overriding consideration of value for money. Two departmental examining officers - in DHSS and Crown Suppliers - examined the effects of the policies in respect of preferred suppliers.

9.13 At present DHSS interpret Treasury guidelines as meaning that they are expected to award 25 per cent of their orders for wheelchairs to preferred suppliers. In effect, one supplier is guaranteed a share of the business even if it fails to tender the lowest price, the actual price of the order being fixed by reference to other suppliers' bids. The company is an established major wheelchair manufacturer. The current policy, however, gives it a more secure share of the market than its competitors. It also means that DHSS may be paying more for wheelchairs than it otherwise would.

9.14 On the other hand, the examining officer in Crown Suppliers found no evidence that the policy on preferred suppliers resulted in higher prices. There is evidence, however, that it added to the cost of procurement, mainly through poor delivery and the unusually high degree of supervision required for some of these suppliers. This additional cost cannot be quantified exactly, though the examining officer's report does give some illustrations of the additional staff time involved.

9.15 Like the DHSS examining officer, we believe that the implications of policies directed towards giving preference to suppliers need to be considered in the wider context of government purchasing. The issue is not the policies themselves but who should be paying for them and by what method. In line with the FMI, we believe that the departments sponsoring the policies should meet any additional costs. But these, as indicated above, are difficult to estimate at present. Using the information systems described in Chapter 7 departments should identify these costs and, if they feel that they are failing to get best value for money because of the application of the policies, they should inform the sponsoring department and consider taking up the case with the Treasury.

EC and GATT rules

9.16 European Community Commission directives require that all UK Exchequer body and local authority supplies contracts worth more than £118,000 are advertised in the *Official Journal* so that European companies can tender for the job. The level is reviewed regularly. In the case of works contracts the level is set higher, currently £590,000. Similarly the GATT rules require all central government and Post Office contracts worth more than £104,000 to be advertised, so opening the tendering to international competition. There are exceptions to both arrangements, the most important of which relates to the purchase of military equipment.

9.17 In practice, examining officers found that the requirement to advertise internationally was, at most, a minor irritation adding on average 6 to 8 weeks to the tendering process. If departments consider that the cost or delay is a matter of concern they should raise the issue with AP Division in the Treasury. In a properly planned purchasing system, the procedure itself should not cause any difficulty. The procurement plan will identify purchases covered by these rules. The service agreements between end-users and the purchasing organisation will specify the lead-time needed to complete the required procedures. It is the responsibility of the end-user to start the purchasing process sufficiently early to guarantee that he can meet his requirements on time.

R B BROWN)
R D J WRIGHT) CABINET OFFICE (MPO)
C G CLOKE)
T B MORRIS
I F S TRUMPER
July 1984

ACKNOWLEDGEMENTS

Outside companies visited

British Airways	Heathrow
British Oxygen Co Ltd	Brentford
Debenhams plc	London
IBM (UK) Ltd	Portsmouth (Havant and North Harbour), Greenock
ICI plc	London, Billingham, Wilton
Marks & Spencer plc	London
National Coal Board	Doncaster
Shell (UK) Ltd	London (Shell-Mex House and Wellington House), Aberdeen, Wilmslow

Organisations

Association of Independent Businesses
Confederation of British Industry
Council of Civil Service Unions
Institute of Purchasing and Supply
National Audit Commission
National Audit Office
National Chamber of Trade
National Economic Development Office

Others

Campbell Christie, Joint Chairman Office Equipment Sector Working Party,
NEDC
Gerald Frankel, Chairman British Micrographic Manufacturer's Association
Erik Fischer and colleagues, State Purchasing Department, Copenhagen,
Denmark.

The 68 companies, and the staff involved, who responded to our questionnaire.



FOREIGN AND COMMONWEALTH OFFICE (FCO)

Area covered: Communications Division - technical equipment and supplies

Examining Officer: Arthur Watson Cost of study: £19,288

	Spend £m	Staff/Admin Cost £m	No. of Staff
Value of area covered	10 - 12	0.21	22½
Potential savings*	0.38	0.06	8
As percentage	3½%	29%	36%

In addition £991,000 once-for-all savings are identified, of which £891,000 have already been achieved. From the stores area savings of seven posts (£43,200) were also identified.

* Including savings from lower prices

Main recommendations

- procurement section responsibilities to be clarified and reaffirmed;
- clarification of service levels to be provided by procurement section; performance targets to be set; channel for end-users to challenge shortfalls in procurement section performance;
- reduction in unnecessary checking; delegation of authority for expenditure;
- procurement information to be improved;
- information on spares usage to be generated and used in lifetime costing analyses;
- delegation of routine work in procurement section; managers to concentrate on setting up call-off and running contracts to maximise benefits from aggregation;
- improved communications with suppliers;
- tender offers to be regarded as the starting point for further negotiation;
- enforcement of contracts;
- target price reduction of 2 per cent on quoted prices under £1,000 rising to 5 per cent on contracts over £50,000;
- revision of inter-departmental procurement service charges.

MANAGEMENT IN CONFIDENCE

DEPARTMENT OF HEALTH AND SOCIAL SECURITY (DHSS)

Area covered: Wheelchair purchase and repair

Examining Officer: Roy Cunningham Cost of study: £13,000

	Spend £m	Staff/Admin Cost £m	No. of Staff
Value of area examined	22	0.5**	50
Potential savings*	1.00	UQ	UQ
As percentage	4.5%		

(A further £350,000 savings depend on policy changes)

*Including savings from lower prices

**Relates to purchasing staff only

Main recommendations

- rationalisation of the method of providing wheelchairs to disabled people having regard to the quality of service and value for money;
- better management information on the costs of spares and repairs;
- rationalisation of stores;
- increased use of call-off contracts;
- greater use of penalty clauses in contracts;
- greater use of investment appraisal and life-time costing technique;
- development of target prices to assess tender bids;
- closer understanding with industry to improve competitiveness of product, including
 - better timing of orders
 - greater use of performance specifications
 - longer term contracts;
- introduction of post-tender negotiation with successful tenderers;
- target of 5 per cent reduction in prices for wheelchairs in 1985;
- target of 10 per cent reduction in the present cost of repairs.

MANAGEMENT IN CONFIDENCE

OVERSEAS DEVELOPMENT ADMINISTRATION (ODA)

Area covered: Goods purchased under the Bilateral Aid Programme

Examining Officer: Mrs Judy White Cost of study: £18,744

	Spend £m	Staff/Admin Cost £m	No. of Staff
Value of area examined	57	3.1	Nil**
Potential savings*	3.2	0.24	
As percentage	5.6%	7.6%	

*Including savings obtainable from lower prices

** ODA use agents

Main recommendations

- procurement of goods under the Technical Co-operation Programme should be transferred from the Crown Agents to the ODA;
- delegation of responsibility to Technical Co-operation Officers for expenditure up to £1,000 on essential goods and services;
- streamlining of communications between ODA and Technical Co-operation Officers;
- Crown Agents should seek discounts on the basis of the volume of business placed with individual suppliers;
- competition amongst procurement agents under the capital aid procurement programme;
- Crown Agents should broaden range of invitations to tender;
- Crown Agents should negotiate with suppliers.

MANAGEMENT IN CONFIDENCE

HOME OFFICE (HO)

Area covered: All Home Office direct procurement (ie excluding that by Police and Fire authorities)

Examining Officer: Robert Fulton Cost of study: £28,765

	Spend £m	Staff/Admin Cost £m	No. of Staff
Value of area covered	133	6.23	UQ
Potential savings*	3.3	0.6	50
As percentage	2.5%	9.6%	

*Including savings obtainable from lower prices

Main recommendations

- rationalisation of authority levels;
- more streamlined procedures for small orders;
- greater flexibility in procurement methods to improve value for money;
- better central co-ordination of purchasing, including monitoring of national contracts;
- wider use of central contracts and better co-ordination with other government departments;
- information technology should be introduced on a comprehensive basis into purchasing and stock control;
- greater use should be made of investment appraisal techniques;
- greater use of suppliers in developing specifications;
- purchasing should be regarded as a specialised function, needing a postings policy that will encourage the development of expertise;
- more training for purchasing staff;
- the PPI should be integrated into a new set of purchasing rules emphasising the objective of "best value for money" over the present "cheapest to specification".

MANAGEMENT IN CONFIDENCE

CENTRAL COMPUTER AND TELECOMMUNICATIONS AGENCY (CCTA)

Area covered: Procurement and Contracts Division (purchase, rental and maintenance of computers)

Examining Officer: Andrew Partridge Cost of study: £13,418

	Spend £m	Staff/Admin Cost £m	No. of Staff
Value of area covered	163	1.62 **	125 †
Potential savings*	8.25	0.275 (net)	26½
As percentage	5%	17%	21%

*Including savings obtainable from lower prices

** including £0.22 million in respect of finance staff

† including 25 from finance division

Main recommendations

- standing arrangements to be set up where cost effective;
- tender evaluation procedures to be streamlined;
- contracts to invoke liquidated damages for late delivery;
- performance indicators to be developed for procurement and contracts division;
- involvement of procurement and contracts division in departmental procurements to be reduced and more closely defined;
- departments to assume responsibility for post-contract discussions with suppliers;
- departments to take responsibility for payment of invoices;
- departments to take responsibility for contracts administered on their behalf by CCTA;
- costs of CCTA advice and support to be recovered on a basis more closely related to the effort involved from 1 April 1986.

MANAGEMENT IN CONFIDENCE

HER MAJESTY'S STATIONERY OFFICE (HMSO)

Area covered: Print Procurement and Supply (stationery, office machines etc)

Study Team: Mick Moore, Mike Cuming, Peter Standley

Cost of Study: £23,750

	Spend £m	Staff/Admin Cost £m	No. of Staff
Value of area examined	195	3.1	336 †
Potential savings*	UQ **	0.5	60
As percentage		16.1%	17.9%

† Number of staff with powers to sign purchase orders

* Including savings obtainable from lower prices

**Unquantified but at least several hundred thousand pounds

Main recommendations

- clarify responsibilities with customers for procurement and supply and rationalise authority levels;
- extend use of call-off and period contracts;
- greater use of information technology throughout purchasing;
- increase use of performance specifications;
- refine specifications to meet more closely end-users' requirements, in particular review quality of printing paper;
- better training for buying staff and greater motivation for better performance;
- experiment with the use of post-tender negotiation during 1984;
- improve performance indicators on prices offered to departments and on the effectiveness of buyers;
- rationalisation of the range of goods and services made available by HMSO, displayed in a more comprehensive catalogue;
- review customer agreements with departments;
- refinement of prices to support more clearly the marketing strategy;
- rationalization of products supplied jointly by HMSO, Crown Suppliers and CCTA;

MANAGEMENT IN CONFIDENCE

CROWN SUPPLIERS (CS) (PSA SUPPLIES UNTIL 18.1.84)

Area covered: All procurement

Examining Officer: William Chapman Cost of Study: £19,288

	Spend £m	Staff/Admin Cost £m	No. of Staff
Value of area covered	500	9.75	520
of which: fuel	283	0.5	20
Potential savings*	4	UQ	UQ
As percentage	0.8%		

* Potential saving of up to 2½ per cent on one-third of purchases from post-tender negotiation.

Main recommendations

- simplification in the tendering and contract procedures;
- reduce specifications where possible;
- introduce agreements between Crown Suppliers and departments to cover quantities required, delivery dates and target prices;
- make efforts to expand approved list by use of booklet for small firms;
- introduce "black mark" system for poor performance by suppliers;
- use information technology both to improve the list of approved suppliers and to provide management information;
- set up and monitor a three month experiment on post tender negotiation;
- introduce performance indicators for purchasing staff.

MANAGEMENT IN CONFIDENCE

DEPARTMENT OF TRANSPORT (DTp)

Area covered: Highways contracts

Examining Officer: Michael Endacott Cost of Study: £29,850

	Spend** £m	Staff/Admin Cost £m	No. of Staff
Value of area examined	683	3.32	UQ
Potential savings*	68	0.96	67
As percentage	10%	29%	-

* Including savings from lower prices

** Including consultants' fees

Main recommendations

- increase delegation to regional offices, in particular by eliminating unnecessary reference to headquarters;
- streamline checking procedures by application of new technology;
- improve feedback on contractor performance;
- eliminate redundant internal financial check procedures;
- set target construction costs and relate consultants' fees to achievement of them;
- experiment with inviting contractors to tender their own completion date proposals and cash flow requirements;
- contractors to specify unit costs for unforeseen variations before work commences;
- negotiate after tenders, where last minute specification changes so require, with only the lowest tenderer;
- adopt a more commercial attitude to contractors generally;
- economise in accommodation for site staff.

MINISTRY OF DEFENCE (MOD)

Area covered: Headquarters non-warlike purchasing

Study Team: Errol Grieve Cost of Study: £60,000
Pat Doherty
Alistair Parker
Duncan O'Neil

	Spend £m	Staff/Admin Cost £m	No. of Staff
Value of area examined	720	4	269
Potential savings*	5 **	0.47	44
As percentage	0.7%	11.7%	16.0%

* Including savings obtainable from lower prices

** Savings of £190,000 were achieved by the date of the report. On the basis of these results there is potential for further savings which are in the range of £5 million (HQ non-warlike purchasing) to £14 million (all competitive tendering).

Main recommendations

- rationalisation of general stores purchasing between the three contracts directorates;
- establishment of additional small value order cells (SVOC) for purchase of appropriate ranges of general stores;
- greater co-ordination of requirements so that better aggregation of purchasing is achieved;
- wider use of existing enabling arrangements within MOD and by other departments;
- greater use of information technology throughout purchasing;
- greater exchange of information between departments about purchasing;
- more encouragement to contracts staff to challenge specifications;
- alternative training for contracts staff to be considered and evaluated;
- measures to increase competition;
- the experiment on post-tender negotiation should continue and be evaluated;
- clearer guidance on Public Purchasing Initiative.



PUBLIC PURCHASING POLICY GUIDELINES

Note by the Treasury (issued 17 March 1981)

1. Departments will know that the Government has recently reviewed its public purchasing policy.
2. The attached guidelines set out steps to be taken in pursuit of this policy. They also include a checklist of factors to be taken into account in reaching procurement decisions and a note on how these factors should be assessed in individual cases. Departments are requested to circulate these guidelines to purchasing officers at all levels and to incorporate them, as appropriate, into their internal contractual instructions. In doing so, departments should ensure that adequate arrangements are made to ensure that there is supervision, at an appropriately senior level, of these procedures and that, where necessary, the Treasury and/or the Department of Industry are consulted.
3. Reference is made in the guidelines to the Treasury's booklet, *Investment Appraisal and Discounting Techniques and the use of the Test Discount Rate in the Public Sector*.¹
4. Departments are also requested to bring these guidelines to the attention of bodies for which they are responsible. The co-operation of local authorities and nationalised industries is also being invited in pursuit of the Government's objectives.

PUBLIC PROCUREMENT POLICY: GUIDELINES

1. It is the Government's policy that, as a matter of enlightened self-interest, public sector purchasers should use the influence their purchases give them to help develop the design, technology and competitiveness of their suppliers.
2. The procurement practices needed to ensure that the Government's policy has the maximum effect are as follows:
 - a. the adoption of a clarified "value for money" criterion;
 - b. the use of best purchasing practices in relations with suppliers;
 - c. clear instructions to public sector purchasers to ensure that the policy is carried out.

Value for money

3. The individual purchaser's objective is to purchase what is needed at the right time and in such a way as to ensure the best value for money. Value for money has sometimes been judged within the context of each individual purchase without taking into account the broader cumulative effect which public sector purchasing can have on the efficiency of suppliers.
4. Value for money should not be judged solely on the basis of the lowest initial cost. Design, reliability and maintainability, for example, will affect the total cost over the life of a product. Factors such as these may justify a higher initial

¹ HM Treasury, 1981.

cost. Actions to promote the industrial viability and hence the trading competitiveness of suppliers can justify an additional initial cost or greater technological risk if over the longer term the purchaser expects to gain improved value for money.

5. The annex to these guidelines provides advice on the factors which may be relevant to individual decisions, and on how they should be assessed.

Enlightened procurement procedures

6. There are a number of practices which public purchasers can adopt. These include:

- a. early dialogues about possible requirements with potential suppliers (including the manufacturers of major components). Such dialogues are more likely to be relevant for large or important contracts, especially those incorporating new or improved technology than for low volume orders for everyday products;
- b. encouraging both product and process innovation;
- c. specifying requirements in performance terms rather than specifying detailed designs which take no account of other industrial applications;
- d. maintaining as far as practicable an even ordering pattern to allow efficient production planning;
- e. de-briefing suppliers on request (within the bounds of commercial confidentiality) when a major contract has been placed elsewhere, including the identification of specific deficiencies in bids.

Dissemination

7. The practices outlined in these guidelines are already part of best practices in both the public and private sectors. Economies of long-term benefit both to suppliers and to purchasers can be achieved through rationalised requirements, more organised volume production and through improvements in production planning. But the principles have not been applied widely enough. It is essential, therefore, that the approach set out in these guidelines becomes an integral part of procedures for the award of public sector contracts.

VALUE FOR MONEY: A CHECKLIST OF FACTORS RELEVANT TO PROCUREMENT DECISIONS

Short-term considerations

1. STATUS OF FIRMS INVOLVED

- Financial viability
- Design capability
- Production capacity
- Quality assurance status and track record
- Cost management arrangements and track record
- Delivery record

2. EQUIPMENT OFFERED

- Extent to which it meets *minimum* requirement
- Design/artistic qualities (where appropriate)
- Compatibility with equipment already in use
- "Extras" above minimum requirement which offer cost-effective advantage
- Scope for improvement or "stretch" by later modifications or "add ons" etc
- Conformity with standards (national, international, NATO etc)
- Scope for value engineering
- Reliability - proven record?
- Maintainability
- Defect reporting and rectification arrangements
- Repair/servicing arrangements

3. IMMEDIATE COST OF ACQUISITION

- Initial price
- Firmness of price (eg fixed, with or without variation of price, cost plus etc)
- Basis for agreeing prices on associated or follow-on orders
- Differences in cost escalation formula
- Foreign exchange risks and costs
- Payment terms (on delivery or progress/stage payments etc)
- Cost of financing interim payments
- Financial guarantee requirements
- Duties and taxes
- Credit terms
- Transport costs
- Installation costs
- Cost of working capital for stocks
- Discounting factors
- Differences in administrative cost (including overheads) to purchaser
- Warranties and technical guarantees offered
- Product liability arrangements
- Scope for, and cost of, accelerating or delaying procurement

4. DELIVERY

- Conformity with requirement
- Reliability of offer
- Operation and financial effects of earlier/later availability
- Cost and trade-offs with stockholding costs at various locations
- Liquidation of damages

Medium-term considerations

5. OPERATING COSTS

- Running costs
- Cost of spares - present and future
- Servicing and maintenance costs
- Storage and other support costs

6. PRODUCT SUPPORT

- Quality of after-sales facilities
- Ease of legal recourse to supplier

7. REPLACEMENT ARRANGEMENTS

- Receipts from eventual disposal
- Commitment to particular replacement equipment
- Replacement timeframe

Longer-term considerations

8. STRATEGIC AND STRUCTURAL

- Safeguarding of vital sources of supply
- Length of the supply chain and its vulnerability to disruption
- Offset considerations
- Effect of procurement on price, availability and competition for future supplies (eg arising from dumping or artificially depressed quotations) including, as appropriate, supplies for other public purchasers.

How these factors should be assessed in individual cases

In evaluating alternative tenders, departments should compare the costs and the receipts (or other benefits) of all those factors which can be quantified in money terms, as in an investment appraisal.¹ The detail, and the precision, of such calculations should reflect the size of the purchase. An elaborate analysis for relatively small contracts would not be appropriate. But contracts for major investments should be analysed in detail, possibly using sensitivity analysis.² At present the discount rate used by departments for comparing costs and benefits which will occur at different points in time is 5 per cent, taking today's prices as constant.

Calculations along these lines provide a comparison between tenders, at constant prices, of those factors which can be quantified. However there will also be factors relevant to a contract which cannot be quantified. Departments should decide, on a case by case basis, how the weight of such additional factors affects the balance between tenders. In those instances where such factors are considered to outweigh the difference between tenders, Departments should indicate clearly on file the nature of the factors which led them to take their purchasing decision.

In any cases of doubt about the industrial implications of individual contracts, departments might wish to consult sponsor divisions of the Department of Industry.

Example A: Purchase of a piece of equipment with a life of 5 years

- (1) All values expressed at constant prices
- (2) discount factors from Annex B of the Treasury booklet (5%)

Tender A initial cost	£100,000
cost of spares	£10,000 a year in Years 2 to 5
Tender B initial cost	£120,000
cost of spares	£5,000 a year in Years 2 to 5

¹See two examples below. Further guidance on the approach to be used is available in the Treasury booklet *Investment Appraisal and Discounting Techniques, and the use of the Test Discount Rate in the Public Sector*.

²Sensitivity analysis involves no more than checking to see how sensitive the evaluation is to alternative assumptions. Its use is described in paragraph 19 of the Treasury booklet.

MANAGEMENT IN CONFIDENCE

Present Value of Tender A

		£
Initial cost		100,000
Spares	£10,000 in Year 2 x .907	9,070
	£10,000 in Year 3 x .864	8,640
	£10,000 in Year 4 x .823	8,230
	£10,000 in Year 5 x .784	7,840
		<hr/>
		133,780
		<hr/>

Present Value of Tender B

Initial cost		120,000
Spares	£5,000 in Year 2 x .907	4,535
	£5,000 in Year 3 x .864	4,320
	£5,000 in Year 4 x .823	4,115
	£5,000 in Year 5 x .784	3,920
		<hr/>
		136,890
		<hr/>

Although the undiscounted values of both contracts (initial cost plus spares) are the same, Tender A is cheaper - allowing for the difference in timing of payments.

Example B: Benefit at a later date equal to extra cost now

What cost benefit would be required in each of Years 6 to 10 to equal payment of an extra £100,000 on a contract now?

Discount factors for Years 6-10 = $.75 + .71 + .68 + .65 + .61 = 3.40$
 $£100,000 \div 3.40 = £29,400$ in each year at present day prices



CONTRACT CONTROL DOCUMENT

1. The purpose of a Contract Control Document is to clarify responsibilities to ensure that all necessary steps are completed prior to the issue of invitations to tender for a contract and to provide a record of authorities and approvals. It can also serve as a useful source of data for the procurement information and management information systems.
2. An example of a Contract Control Document, based in part on one used by a large private sector company, is at Appendix 1. This would need to be adapted to suit individual departments' requirements. At Appendix 2 is a copy of the Purchase Record form developed by the Home Office examining team: this provides an example of how the concept of the Contract Control Document might be adapted to provide a record of local purchase decisions in a widely dispersed purchasing organisation.
3. Departments will need to develop Contract Control Documents appropriate to the purchases they make. They may need to develop different control documents for different types of purchase: for example a purchase record on the lines of that at Appendix 2 may be sufficient for local purchasing, but more detailed documents may be required for large volume call-off contracts or for major project contracts. It is important that the control document suits the type of procurement being undertaken as well as the organisational arrangements for procurement within each department. The document at Appendix 1 is intended to serve as a model for departments' own documentation: it is not meant to be prescriptive.

Key features of the model Contract Control Document

4. Section 1 of the document provides basic background information on the procurement being undertaken. It identifies the sponsoring officer responsible for requesting the purchase (the "end-user" in the terms of the main body of this report) and describes the requirement. This section would be completed by the sponsoring officer.
5. Section 2 of the document outlines the financial backing for the purchase. A key feature of this section is the requirement on the sponsor, in consultation with the purchasing section, to estimate the price of the good or service requested prior to tender (2(b)) and to estimate the likely overall cost of the contract (2(c)). This places the onus on the sponsor and the purchasing organisation to quantify on-costs and likely variation costs before inviting tenders. These costs will influence the contract strategy adopted by the department. Section 2(d) of the document provides a record of the cost centre manager's approval of the commitment to spend the total contract cost at 2(c).
6. Section 3 of the document outlines the contract strategy. Again, the emphasis here is on ensuring that all necessary steps have been taken, decisions made and approvals given before inviting tenders. Section 3 would be completed by the sponsor in consultation with the purchasing organisation who, together, will recommend the contract strategy to senior management (3(i)) for approval (3(j)).
7. Parts 3(c), (d) and (e) require the sponsor and the purchasing organisation to determine in advance the basis upon which suppliers will be invited to tender. The sponsor is required to justify his reasons if he wishes to recommend single tender action or to invite tenders on a cost-plus price basis, either of which can have major repercussions on costs to the department.

8. At 3(f) the sponsor and purchasing organisation will be required in advance to assess the likely value of post-tender negotiation with the best bidder.

9. Before issuing invitations to tender, the sponsor should be required to indicate the basis upon which bids will be evaluated and compared. This evaluation plan will normally indicate the relative importance that will be attached to the main parameters of cost, quality and timeliness. Other considerations may also play an important part in evaluating bids and these should be indicated in this section of the document. It might, for example, in some circumstances be particularly important for the department to avoid the creation of a technical monopoly - in which case preference might be given to any acceptable bid from a new supplier. Or the department may wish to break up the contract in order to preserve a competitive manufacturing base.

10. Once the strategy has been approved by senior management, the procurement procedure progresses according to that strategy. Section 4 of the document provides a formal record of the proper conduct of the tender opening process, if appropriate.

11. Section 5 of the document summarises the recommendation to award the contract to a particular supplier or contractor and certifies the approval of the recommendation for action. At 5(b), the contract price is shown. Comparison of this price with the sponsor's pre-tender price at 2(b) will provide a measure of the effectiveness of the activities of the sponsor and the purchasing organisation. The sponsor is also required to indicate, in the light of tenders received, a revised estimate of the overall contract cost. Comparison of this figure with the pre-tender estimate at 2(c) will provide a measure of the effectiveness of the procurement strategy adopted.

12. Any increase over the pre-tender estimates would need to be justified to senior management. Similarly, if the post-tender price and estimated cost were significantly lower than the pre-tender estimates, management would need to investigate. Such a result might indicate failings in the estimating procedure or that, for whatever reason, the suppliers' bids did not fully reflect the department's needs. These figures therefore provide a useful means of assessing the procurement process as a whole and act as a spur to both the sponsor and the purchasing organisation to encourage them to consider all cost implications in advance of the tendering process.

13. If a contract is subject to variation clauses, senior management may wish to review the contract as it progresses. At Section 5(d) senior management, before approving the award of the contract, can indicate the level of expenditure at which they would require the contract to be reviewed and possibly, if appropriate, re-let.

Other purposes

14. The Contract Control Document, as described above, can prove a very useful tool for management control. As well as providing a basis for record-keeping in respect of individual contracts, it can also provide key inputs to the procurement and management information systems (this, for example, is one of the main purposes of the purchase record at Appendix 2). For example, if a series of purchases were to be placed by one sponsor with a particular supplier on a regular basis, or if a sponsor were repeatedly to propose letting contracts by single-tender action with one supplier, senior management would need to investigate whether this was prima facie evidence of the build-up of a technical monopoly. The contract control documents, by providing a summary of all aspects of the contract, can readily provide a source of useful data for the procurement and management information systems of the department.

Signatures

15. A completed Contract Control Document will contain many signatures. It is essential, for proper control and to protect those who sign, that departments make clear what these signatures denote. We think there is much to be said for attaching a clear statement of responsibilities to the Contract Control Document. We envisage this statement taking the following form:

"RESPONSIBILITIES

The **sponsor** signs to say:

- that the contract strategy and documents as prepared are consistent with his objectives as to time, cost, quality, and technical compatibility; and
- that all relevant internal functions have been consulted on technical matters and that all other relevant departmental procedures have been observed.

The **buyer** signs to say:

- that the contract documents as prepared are acceptable and consistent with the department's policies; that they allocate risks clearly as between the department and the supplier; and that the elements of the contract designed to protect the Exchequer's interest are enforceable;
- that the financial standing of the contractors invited to tender has been commercially evaluated as appropriate for the contract work envisaged; and
- that the commercial and financial basis for the contract strategy is supported as being likely to maximise value for money.

The **cost centre manager** signs to say:

- that he has obtained budget approval sufficient to cover the likely or actual commitment of expenditure.

If necessary (eg because the buyer lacks final authority at that level of expenditure) the **senior buyer** signs to say that he approves the contract strategy in the terms set out above for the buyer.

If necessary (eg because the senior buyer lacks the final authority at that level of expenditure), the **responsible officer in the Finance Section** would sign to say that he approves the contract strategy in the terms set out above for the buyer.

... etc"

Model Contract Control Document

Section 1 : Background

- (a) Contract Title
- (b) Contract No.
- (c) Project No. (if appropriate)
- (d) Originating Division
- (e) Responsible Officer (Sponsor)
- (f) Requirement (attach specification if appropriate)

Section 2 : Finance

- (a) Chargeable Cost Centre
 - (b) Sponsor's pre-contract estimate of tender price (not for disclosure to tenderers) : £ _____
 - (c) Sponsor's pre-contract estimate of overall contract cost (attach schedule of on-costs and variation costs as appropriate) : £ _____
 - (d) Commitment approved
- (Cost Centre Manager's signature)

Section 3 : Contract Strategy Please tick appropriate boxes

- (a) Sponsor's required delivery date : (earliest): (latest): (attach schedule if appropriate)
- (b) Issue of invitations to tender : (date) Bids due in : (date)
- (c) Investment appraisal complete : (date) File No.
- (d) Terms of supply : fixed price cost plus day works other
- open tender multiple tender single tender
- purchase hire lease
- GC works 1 GC stores 1 Other call-off direct supply consignment
- (e) Sponsor's reason if single tender
- (f) Sponsor's reason if cost plus
- (g) Post-tender negotiation: Yes No Reasons

MANAGEMENT IN CONFIDENCE

(h) Invitations to tender:

	Supplier	Code		Supplier	Code
1			5		
2			6		
3			7		
4			8		

(i) Proposed basis for evaluation/comparison of bids

.....

(j) Contract strategy recommended

(sponsor's signature) (date)

.....

(buyer's signature) (date)

(k) Contract strategy approved

(senior buyer's signature) (date)

.....

(responsible officer, Finance) (date)

Section 4 : Tender Opening

(a) Tenders recorded

(signature of responsible officer) (date)

Section 5 : Recommendation

(a) Award contract to

(b) Contract price : £ (c) Sponsor's estimated overall contract cost : £ (d) Review limit : £

(e) Recommended by :

(sponsor's signature) (date)

.....

(buyer's signature) (date)

.....

(responsible officer, Finance) (date)

.....

(other) (date)

(f) Approved by :

(cost centre manager's signature) (date)

.....

(senior buyer's signature) (date)

.....

(authorised signatory) (date)

(g) Contract awarded : (date) ; by :

(signature of officer signing contract)

(h) Unsuccessful tenderers informed : (date) ; by:

(signature of buyer)



CONTRACT/
ORDER NO.

PURCHASE RECORD

HOME OFFICE (To be completed for all purchases over £500 not covered by existing contract and for all contracts with a labour element)

• When contract has been let, a copy of this form **must** be forwarded to Finance Division 2. The **original** should be retained on the tender file.

• Please tick appropriate boxes

A. CONTRACT

File No.

Division/Directorate etc

Establishment

Description of goods, works or services:

Item Code

Quantity

Officer responsible for project

Officer responsible for purchase

B. FINANCE

Project officer's pre-tender estimate of contract value

£

Subhead

Head of Service

Accounting Code

Project Investment Appraisal

Yes

No

Date carried out

File reference

C. PROCEDURE

Contract period

Start

Finish

Contract Type

Firm price

Cost plus

Form of Contract

GC/Works/1

GC/Stores/1

Other

Special conditions:

Type of procedure

Formal tender

Written Quotation

No. of tenders/quotations invited

C. PROCEDURE (continued)

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•Although full explanations should be recorded on contracts file please outline reasons (if applicable) for:

(i) non-use of existing contract:

(ii) single-tender action:

Issue of tenders:	Name	Grade	Date
Proposed by:			
Approved by:			
Single tender action approved by:			
Fin Div 2 approval by:			

D. TENDER OPENING

Tenders opened by and Date

No of tenders received

E. EVALUATION & RECOMMENDATION

Award contract to on grounds of:-

lowest cost best delivery best quality

Results of Investment appraisal (if applicable):

U.K. content % Reasons if less than 100%:

Unit Price of items purchased (if applicable)

Consideration given to (i) Public Purchasing Initiative, (ii) Regional Policy, (iii) Small Firms Policies:

F. AWARD OF CONTRACT

	Name	Grade	Date
Proposed by:			
Approved by:			
Fin Div 2 approval by:			
Successful Tender accepted	Date	<input type="text"/>	Decline letters sent <input type="text"/>

ANALYSIS OF RESPONSE TO QUESTIONNAIRE

1. To obtain suppliers' views on government contract and procurement procedures the central team sent a questionnaire to 125 private sector companies. Sixty-eight companies (54 per cent) responded. These 68 companies supply departments with goods and services worth over £350 million a year.
2. The questions asked are shown below together with an analysis of the responses. We also invited suppliers to comment on their answers. Some suppliers - particularly those who expressed broad satisfaction with government procedures - made none. Others provided many useful views.
3. Drawing conclusions*from so small a sample requires caution. For example, many comments apply solely to the Ministry of Defence since the sample reflected that department's role as the largest purchaser from industry in cash terms and probably product diversity. Moreover, all the responses were from companies who already supply or have supplied to the government.
4. Although most companies expressed reasonable satisfaction with government procedures the comments received reflect a remarkable consensus of views; particularly where we invited views on improvements to help both suppliers and the government reduce costs.
5. It is clear that many of the suggestions would lead to the government securing better value for the taxpayers' money and that suppliers would benefit too.
6. Many suppliers were critical of both the complexity and sheer volume of documentation (including forms) that they were required to deal with. They pointed out the high administrative costs that this incurs to both sides. Equally they found that locating staff who have the necessary responsibility and authority to make prompt decisions was a frustrating and time-consuming business. Some suppliers thought that slow decisions from departments were a direct result of having too many staff involved in the process.
7. In particular, there is a strong indication from the replies that a positive drive for better communication within and between departments, and between departments and suppliers, would bring mutual rewards. Improvements in communication may lead both buyer and seller to a better understanding of each others' needs and objectives and to the establishment of a more effective way of securing the maximum benefit to both sides.
8. Fifteen per cent of the companies responding thought that a change in government tendering procedures, allowing more room for discussion and negotiation, would be mutually advantageous.
9. A summary of the suppliers' responses to the wider questions asked is shown below with the main themes in bold type and companies' suggestions for improvement underneath.

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SUMMARY OF RESPONSES

Frequency
of comment

- 51% **Difficulty in locating people who take decisions, decide specifications etc**
Publish a directory indicating which departments are interested in particular products/services. Show who should be contacted together with their level of authority. Keep staff in jobs longer and, when replaced, give better hand-over briefing; let suppliers know of any changes. Create a forum that allows the presentation of new products and ideas.
- 31% **Administrative burden caused by the high volume and/or complexity of documents**
Allow greater use of commercially acceptable documents, particularly invoices. Rationalise documents and forms and in particular reduce the practice of cross-referencing from one contract document to another.
- 31% **Too many products bought (and packaged) to high quality specifications unique to government. Altering an already established product's specification may incur costs disproportionate to the performance gain**
Buy against performance criteria, not detailed specifications. Use internationally recognised standards where possible. Allow specification/performance flexibility where this significantly lowers costs. Avoid "gold-plating". Appreciate that special design features and specifications may inhibit a product's chances of success overseas.
- 28% **Poor planning, resulting in need for urgent supplies, loss of savings through not aggregating orders, specification/design changes during manufacture**
Plan ahead, with suppliers if possible. Notify suppliers of tender requirements earlier. Make best use of savings available through aggregating orders and avoid the risk of minimum order charges. Freeze design and specification at start of contract.
- 18% **Delays in decision-making in (and between) departments**
Reduce the number of people involved in the decision-making process. Improve inter-departmental liaison.
- 15% **Quality control and testing procedures**
Avoid duplication. Leave the responsibility for quality control to manufacturers where track records are already proven. Encourage those less proficient in this area to improve. Make use of BS 5750.
- 15% **Tendering procedures inhibit negotiation**
Allow negotiation, thereby creating a more flexible and mutually advantageous buyer/seller interface.
- 12% **Insufficient feedback on failed tenders, too much secrecy**
De-brief unsuccessful tenderers in more detail. Avoid unnecessary secrecy (eg who won a contract).
- 9% **Slow agreement on prices by contracts sections, thereby incurring higher finance costs to suppliers and reduction of cash flow**
Agree prices quickly, extend the use of progress/stage payments.
- 9% **All too often contracts seem to be awarded solely on price**
Buy lowest cost, not price. Give other criteria appropriate consideration (eg past performance). Take long-term costs into account.

MANAGEMENT IN CONFIDENCE QUESTIONNAIRE

Procedures

- | | |
|--|------------------------|
| 1. Do you find that the procedures of government departments are significantly different from those of your other customers? | Yes: 62% No: 35% |
| 2. If you answered yes to question 1, please give examples of how government procedures differ. Please say whether they make supply easier or more difficult. | See summary Easier: 9% |
| 3. Do you think that any of the documents (for example forms) you have to deal with in order to obtain a government contract cause you or your staff unnecessary work? | Yes: 32% No: 66% |
| 4. If you answered yes to question 3 please give details of the documents you consider are unnecessarily time-consuming | See summary |

Access

- | | |
|---|---------------------|
| 5. Can you promote your company's products and ideas as widely as you would like in central government? | Yes: 60% No: 37% |
| 6. If you answered no to question 5 what obstacles have you come across? | See summary |

Communications

- | | |
|--|---------------------|
| 7. It is the government's policy to promote good communications between government departments and suppliers. Do you think this is successful? | Yes: 74% No: 25% |
| 8. To enable you to quote effectively for contracts put out to tender, is the information provided sufficiently | |
| - detailed? | Yes: 87% No: 10% |
| - timely? | Yes: 81% No: 16% |
| 9. Are decisions on contracts communicated to you promptly? | Yes: 74% No: 24% |
| 10. If you have answered no to questions 7, 8 or 9 please give examples of poor communications below, if possible. | See summary |

Staff

- | | |
|--|--------------------|
| 11. In general do you find government procurement staff in departments | |
| - knowledgeable on contract matters? | Yes: 91% No: 6% |
| - polite? | Yes: 98% No: 1% |
| - responsive? | Yes: 91% No: 7% |

Payment

- | | |
|---|--------------------|
| 12. Does your company receive payment promptly from government departments? | Yes: 89% No: 9% |
| 13. Do you give early payment discounts to government? | Yes: 9% No: 91% |

Background

- | | |
|--|---|
| 14. Please list the government departments which your company supplies | MOD, HMSO, MAFF, COI, ODA, DOE, DHSS, DTP, HO, PSA, C&E, DEn, DI, IR. |
| 15. What was the approximate value of your company's sales to government in its last financial year? | Total of all companies who replied: £350 million |
| 16. What was your company's turnover in its last financial year? | Varied between £½ million and £4 billion |

Improvements

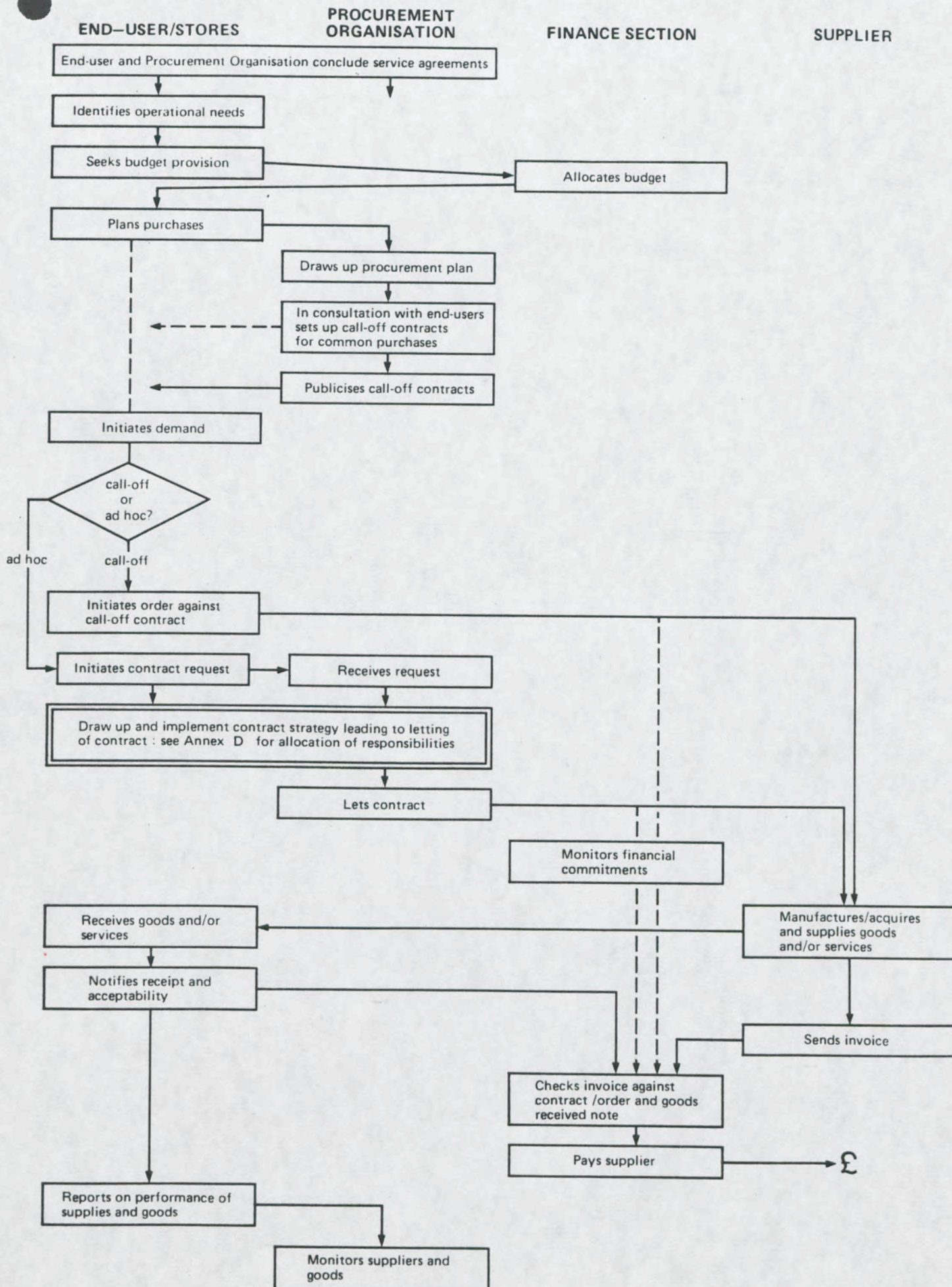
- | | |
|---|---------------|
| 17. Please list below any ideas you, as a supplier, may have on how procurement by government departments could be improved | |
| - to reduce costs? |) see summary |
| - and to reduce the cost to the taxpayer? | |



MANAGEMENT IN CONFIDENCE

TYPICAL PROCUREMENT ARRANGEMENTS, CHECKS AND RECORDS

ANNEX F





ROLES AND RESPONSIBILITIES OF THE DEPARTMENTAL PROCUREMENT AND SUPPLY ORGANISATION AND END-USERS

The first section of this Annex might form the basis of a formal job description for the departmental Director of Procurement and Supply. From it, the Accounting Officer might wish to derive annual performance targets for the Director of Procurement and Supply and his/her organisation.

The procurement and supply organisation: responsibilities

The aim of the departmental procurement and supply organisation is to provide end-users with access to the goods and services that they need, when they need them and at least cost. The organisation is responsible through the Principal Finance Officer to the Accounting Officer for maximising value for money in procurement and supply across the department and, by means of appropriate managerial and contractual arrangements, for protecting the Accounting Officer's interests in procurement.

The procurement and supply organisation will be responsible for the following:

- developing and maintaining appropriate procurement planning arrangements in order to identify common goods and services;
- providing information to potential suppliers on future requirements; discussing emerging needs and how these might best be met (including scope for collaboration between purchaser and supplier in developing new products); and discussing specifications with potential suppliers;
- negotiating contracts with suppliers;
- improving the efficiency and effectiveness of the procurement and supply organisation so as to minimise the overall cost of meeting end-users' requirements;
- concluding service agreements with end-users that clearly allocate responsibilities in procurement and commit the procurement organisation to pre-agreed levels of service;
- challenging non-standard end-user specifications, in order to minimise inessential differences between specifications; to maximise cost-effective commonalities amongst specifications; to encourage the use of standard products, performance specifications and internationally-acceptable standards; to achieve the most economical match between specification and operational need; and to achieve the most economical match between operational need and the ability of suppliers cost-effectively to meet that need;
- maintaining and reviewing approved lists;
- developing a close understanding of the markets from which the organisation buys goods and services in order to inform end-users of new potential suppliers and new developments, for example in manufacturing processes;

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- promoting the adoption of BS5750, through giving preference where appropriate to suppliers who have achieved certification to an appropriate level;
- developing and maintaining an effective procurement information system which holds data on the department's historic, current and future procurement needs, together with information on suppliers who might be able to meet those needs;
- developing and maintaining a management information system for the procurement organisation that provides an effective basis for monitoring the performance of the organisation and of individuals within it;
- establishing contract control procedures that require setting pre-tender target prices; justifying exceptions to competitive tender arrangements; justifying action taken in the absence of an appropriately sophisticated investment appraisal; and predetermining the most appropriate contract strategy for each procurement;
- where appropriate, negotiating with the bidder of the most favourable competitive bid in order to secure a better overall deal for the department;
- informing end-users of centrally negotiated call-off contracts and authorising access to those contracts;
- arranging appropriate skill training for buyers;
- reviewing procurement and contract documentation in order to clarify responsibilities and risks.

End-users: responsibilities

- forecasting future needs for goods and services as accurately as possible in the context of departmental procurement planning arrangements;
- specifying the goods and services required to meet operational needs;
- securing budget approval for, and funding, the purchase of goods and services;
- initiating demands sufficiently early to enable the procurement and supply organisation to secure best value for money;
- drawing up, in consultation with the procurement and supply organisation, an appropriate procurement strategy for each procurement;
- informing the procurement and supply organisation of orders placed against centrally negotiated call-off contracts;
- receiving and assessing goods and services purchased, and reporting on timeliness and quality to the procurement and supply organisation.

CENTRAL PURCHASING UNIT (CPU)

PRINCIPAL TASKS

1. **Monitoring Progress** (Chapter 7)

The task set by the report for departments is an enormous one. Their progress towards implementation of the 22 recommendations aimed at them has to be monitored. Departments will need encouragement and help to make the necessary changes. This will be the main task of the CPU.

The CPU will have to get alongside departments in order to assess what progress is being made. That information, together with formal statements by the departmental directors, will enable the head of the CPU to prepare annual reports to the Prime Minister on what is happening. These reports should not only record achievement, but should indicate areas where further effort or work are needed and, if necessary, make recommendations. We see the monitoring role as an active one, closely related to the CPU's advisory function.

2. **Advice** (Chapters 7 & 9)

The need for an injection of private sector expertise into government buying is a theme running through the report. It will be achieved in major departments by appointment or designation of a departmental director with private sector experience. In addition, departments will need help and advice on the practical aspects of buying. The CPU will be well placed to provide this.

Much of the advice given is likely to be informal, perhaps over the telephone. But where common problems arise the unit may wish to write formally to all government procurement organisations with practical help on these. The head of the CPU will wish to decide how to distribute such formal advice and may wish to consider the possibility of regular newsletters to purchasing organisations promulgating best practice.

Recommendation 29 concerns the issue of formal guidance to departments on the practical aspects of buying. It is envisaged this will incorporate and develop the practical aspects of the Treasury guidelines on the PPI and will give practical advice on the use of standards. The guidance should cover such things as the development of a procurement strategy, the use of competitive tendering etc. It should not be prescriptive.

3. **Targets** (Chapter 7)

Departments will be required to draw up targets for achieving savings in administration, stockholdings and prices; and criteria for success in specific projects. These are to be agreed with the CPU. This will be a priority task for the CPU. It will also be charged with reporting to the Prime Minister on progress towards achieving these targets.

4. **Aggregation** (Chapter 3)

The report identifies a need for inter-departmental planning in order to ensure that government gains maximum advantage from its buying power. The CPU should adopt a co-ordinating role. The departmental procurement plans (paragraph 3.7) should be

submitted to the CPU. The unit will analyse these to identify where departments are buying common goods and services not already supplied through the central agencies. To help in this, the CPU may want to establish a simple inter-departmental coding system, drawing on existing ones as appropriate. It should then identify a lead department, which in most cases will be obvious, and request them to draw up a call-off contract which can be used by other departments.

Where these contracts are major ones, particularly those involving post-tender negotiation, the CPU may wish to be involved in setting them up. This could involve working alongside the buying team in the lead department or, if the head of the CPU thought it important that his/her staff retained some practical buying experience, the unit itself might take on the task of setting up the contract.

5. **Standards** (Chapter 2)

Departmental procurement organisations are expected to be conversant with the appropriate standards and to represent the department on the relevant BSI and other standards committees. The White Paper, *Standards, Quality and International Competitiveness* (Cmnd 8621), requires those in central government responsible for drawing up specifications to use internationally accepted standards. In addition, where there are no internationally accepted standards users should work towards the adoption of British ones. There will be occasions on which a number of departments have an interest in the same standards. Co-ordination of their approach to the relevant standards committees is essential if government is to have maximum influence on the development of standards. The CPU should have the responsibility for nominating the lead department in such cases. There may be circumstances in which the CPU itself decides to take the lead and to attend the relevant committee. In determining where the lead should lie, the CPU should consult the relevant division in DTI.

6. **Procurement strategies** (Chapter 3)

Departments will be expected to draw up a framework for the preparation of detailed procurement strategies. The CPU should be available for consultation on this, though responsibility rests with departments. In the light of experience the CPU may wish to draw up guidelines.

7. **Service agreements** (Chapter 5)

Departmental directors of procurement and supply are required to agree with end-users the level of service to be expected. The CPU should be consulted and should advise on model forms of such agreements.

8. **Training of purchasing staff** (Chapter 6)

Departmental directors of procurement and supply are required to draw up a training programme for procurement staff. The CPU will be expected to give general guidance on this, in particular on the use of outside organisations to provide training. In addition, the Civil Service College will wish to devise appropriate courses and the CPU should be involved in this task. The private sector members of the unit will be expected to participate in any courses devised by the College. The CPU should also be involved in discussions with Cabinet Office (MPO) on the career management of procurement staff, including such things as succession planning of senior purchasing posts.

9. **Motivation and incentives** (Chapter 6)

The drawing up of performance targets for buying staff is a matter for individual departments in consultation with the staff involved. Individual departments, and different parts of the same organisation, may need to have different performance criteria. But it would be helpful for the CPU to collect information on the criteria adopted by departments with a view to developing guidelines.

The recommendation for bonus schemes for buying staff should be implemented departmentally on an experimental basis. The trials should be monitored centrally by the CPU in consultation with Cabinet Office (MPO).

10. **Repayment schemes** (Chapter 6)

The report advocates the use of internal repayment schemes as a means of motivating purchasing staff to improve performance. It recognises the practical difficulties of such an arrangement. Further work is suggested and this would fall to the CPU in consultation with the Treasury.

11. **The future of agencies** (Chapter 8)

The report suggests that further consideration should be given to the number of government central procurement agencies. It is proposed that the heads of the agencies, the head of the CPU and the central departments consider this once the recommendations in Chapter 8 have been implemented.

12. **Small firms** (Chapter 9)

From departmental procurement plans the CPU should be able to identify those major goods and services which government buy. This information should be passed to DTI to help them prepare revisions of *Tendering For Government Contracts*.¹ The unit should be consulted about the revisions generally. The unit should also promote and devise, in consultation with departments, simpler, standardised procedures and the use of common approved lists.

RELATIONSHIPS WITH OTHER GOVERNMENT DEPARTMENTS

13. The report envisages the CPU being a source of practical advice and help as well as a catalyst for change. It is not seen as a policy making body. The responsibilities for policy on government purchasing should remain with AP Division in the Treasury and with those divisions in DTI currently responsible for the PPI and standards.

14. The CPU's main concern will be with the purchasing organisations in departments but there needs to be close liaison between the CPU and Treasury and DTI in respect of purchasing policy. The CPU should be represented on the Purchasing Policy Committee chaired by Treasury. This is an inter-departmental group which considers policy and other matters relating to procurement. DTI hold regular meetings with NEDO, organisations representing the private sector, including small firms, and other departments on aspects of the PPI. The CPU should be involved in the main meetings.

15. The CPU will also have to develop close relations with Treasury expenditure divisions over the setting of departmental savings targets and over the manpower needs of procurement organisations.

¹ Prepared by the Department of Industry and the Central Office of Information, 1981.

THE POSITION OF THE CPU

16. The report comes to no conclusion about where the CPU should sit in Whitehall. Two main options are available - in one of the existing agencies or at the centre.

17. **Within an existing agency.** The unit could become part of one of the central procurement agencies - HMSO, CCTA, Crown Suppliers. The advantage of this would be that it would be in an organisation whose main business is to carry out effective purchasing. Thus the unit would be able to draw on a wide range of existing expertise.

18. The disadvantage would be that the agency and CPU will have different objectives. The CPU's main aim will be to promote change. The agencies' aim is to service the operational needs of departments and the wider role envisaged for the CPU could detract from this. The report proposes that the agencies concentrate on what they can do best - provide effective purchasing of large volume items - and should thus re-examine the other functions which they carry out at present. It would not be in line with that approach to add to the tasks of one of the agencies. Further, the report envisages the head of the CPU having direct access to senior ministers. If the unit is placed in an agency it would be expected that the head of the unit should report through the agency head to the responsible departmental minister. This could cause difficulties, for example, over the unit's responsibilities in regard to the future of the agencies. If the head of the agency in which the CPU was placed had different views from the unit's head over what should happen in the longer term to the agencies, resolution of these would be difficult if the unit head's immediate line manager was the agency head.

19. **Within the centre** (Treasury, Cabinet Office or an independent unit). The advantages of placing the unit in the centre are that it would be close to policy on purchasing in the Treasury; would fit in well with the traditional monitoring and audit role of Cabinet Office; and would have direct and easy access to senior ministers, as does the Prime Minister's adviser on efficiency. Further, some aspects of the CPU's work will involve helping to resolve conflicts between departments and that may best be done from the centre.

20. We conclude that the unit should be situated in the centre but have no strong views about where in the centre. That would be a matter for ministers to decide.

AGENCIES

1. The central agencies - Her Majesty's Stationery Office, Crown Suppliers, Property Services Agency, Central Computer and Telecommunications Agency and Central Office of Information - arrange for the supply of common goods and services to government departments. During the year to 31 March 1983, it is estimated that departments as a whole spent about £1,700 million through these agencies; this represents about 12 per cent by value of all goods and services bought by government departments.

Agencies in the Review

2. HMSO supplies stationery, office machinery and printing. Crown Suppliers is the largest purchaser of road borne fuel in Europe; they also supply furniture and furnishings, mechanical and electrical equipment and associated services. CCTA purchase computers and telecommunications equipment. Crown Suppliers (then PSA (Supplies)) became a trading fund in 1976 and HMSO in 1980. The Treasury has set both these agencies a financial target of 5 per cent return (in current cost terms) on the average net assets employed. The CCTA is not a trading fund.

3. Departments are formally tied to Crown Suppliers and CCTA - that is, they are expected to buy the goods and services provided by the agencies only from them or on contracts arranged by them. In both cases however, certain relaxations have been introduced which allow departments to buy some low value goods from the most convenient source to them. In the case of HMSO there was formal untying in 1982. However, HMSO then negotiated customer agreements with all departments (except the Department of the Environment). These agreements effectively bind departments to HMSO for specified periods (varying with the product area in question). The argument for these agreements is that they help sustain the advantages of centralised purchasing and to protect the agency's long-term contracts with suppliers and printers. In theory, departments can withdraw from agreements if they can demonstrate to the Treasury that buying from elsewhere would not increase the overall cost to the Exchequer. According to the HMSO report, no department has made use of this provision to date, although a small number conducted market tests before entering into the customer agreements to ensure that HMSO's prices did represent the best available value for money.

4. Both HMSO and Crown Suppliers provide goods and services to public bodies other than government departments. These bodies include the local and health authorities and the nationalised industries. They are not tied in any way to the two agencies. In the year ending March 1983, 37 per cent of HMSO's sales and 40 per cent of Crown Suppliers' was to these customers. As a result of the recent review of CCTA, the agency will be withdrawing its activities on behalf of non-central government bodies.





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ISSUES

We need to tackle three particular issues at an early stage. First, the team recommend (paras 7.9-7.14 and Annex H of the report) the establishment of a Central Purchasing Unit. They see this as an essential catalyst in bringing about the major changes of approach envisaged in their report. I think you will want to accept the recommendation and take an early view on the location of the Unit. Annex H of the report sets out the three options on where the Unit should be situated and you will want to consider these in the light of advice from Sir Robert Armstrong.

Second, the team recommend (paras 7.15-7.24) that individual savings targets are set by departments and agreed with the centre. This approach is common in the private sector. I believe that, properly done, it is a technique we should adopt. Although, as the report says, it will be for departments to set their own targets, I am sure that you will wish to indicate to Ministers the broad levels of savings that they should aim to achieve. Initially that might be the 5% quoted in the report, to be achieved within the first 2 years. But I am confident that is only a start; we should expect further improvements year on year thereafter.

Third, we need to consider the role of the central purchasing agencies - especially HMSO, Crown Suppliers and CCTA. Chapter 8 of the report recommends changes to improve the quality of service provided by these agencies and to give departments greater freedom of choice. The team believe that implementation of this strategy would enable the number of central agencies to be reviewed by the end of the decade. Their proposals raise machinery of government issues and will need more detailed consideration in the context of the other work already being done on the agencies under Sir Robert Armstrong's direction.

HANDLING

This is an important report with major implications for the relationship between government and its private sector suppliers. The bulk of the savings envisaged will come from reducing the real prices we pay for goods and services and from running down government stocks. Industry will be closely interested in the team's proposals - and there is bound to be alarm in some quarters. Robin Ibbs (who has been closely associated with this work throughout) has held confidential consultations on it with a number of leading industrialists. They welcomed the findings which were emerging as a clear exposition of good purchasing practice. They also welcomed the potential savings identified. Interestingly, the recent CBI report 'Efficiency and the Public Service' also identified procurement as an area in which improvements can be made and echoed many of the points in the central team's report. But expressions of general support are one thing; actually living

With a more aggressive and cost-conscious public sector purchaser is quite another. I do not for one moment suggest that we should hold back from achieving worthwhile savings on this account. But presentation will be very important.

As a next step, I recommend that you call a meeting with colleagues to consider the main issues raised by the report, and the question of publishing it. If you agree, I will write to you again, with copies to colleagues, setting out rather more fully the issues for discussion. I would suggest that the Chancellor of the Exchequer, the Foreign and Home Secretaries and the Secretaries of State for Defence, Social Services, Environment, Trade and Industry and Transport should be invited to such a meeting.

For the time being, I am copying this minute only to the Chancellor of the Exchequer, Sir Robert Armstrong and Sir Robin Ibb.

Ge

LORD GOWRIE
3 August 1984

GOVERNMENT PURCHASING: SUMMARY

Central government departments spend around £7,600 million a year on non-warlike goods and services. The report examines the way in which departments buy these goods and services.

2. The report's main conclusion is that the overall costs of purchasing can be reduced substantially. It recommends that departments set targets for savings. If the package of measures advocated in the report are applied to all areas of non-warlike government purchasing, the report concludes that savings of at least £400 million ought to be achievable.

3. Some of these savings will flow from improvements in the efficiency of purchasing arrangements. In particular, the process can be streamlined by reducing paperwork, less double-checking greater delegation of authority and a clearer definition of the level of service to be provided by purchasing organizations to operational divisions. Savings can also be made by reductions in stockholdings, many of which are too high because of poor purchasing decisions made in the past.

4. By far the bulk of the improvements will come from government paying less for what it buys. There are three ways in which this can be done. First, departments need to promote industrial innovation and competitiveness by relying more on performance specifications rather than on detailed descriptions of the goods and services required. Allied to this is the need to adopt internationally accepted standards, which will help industry to compete in international markets.

5. Second, there should be better planning. At present departments generally do not use the available information on what they buy to determine where greater effort needs to be made or where the benefits of aggregation of demand can be exploited.

6. Third, departments should improve their knowledge of supplier and the market. This involves giving more information to suppliers about future needs, discussing with them what is available to meet those needs and, if necessary, explaining to them why their bids for government business have not been accepted. Government buyers have traditionally adopted an arms-length approach to purchasing.

Various techniques used by the private sector, such as product analysis, post-tender negotiation and price targets, should be practised by departments.

7. Improvements in purchasing depend on having the right staff. The report makes recommendations aimed at improving the expertise of staff through identifying the right talent, through secondments to the private sector and by better training. Purchasing staff also need greater motivation. The report proposes establishing performance targets and awarding financial incentives to staff who exceed their targets.

8. The management structure of purchasing needs to be clarified. In particular there needs to be a formal statement of the roles and responsibilities of both the buying department and the end-user (the individual who requires the goods or services to be bought for operational purposes). Within departments there should be a single person designated as director of procurement and supply who will have responsibility for ensuring that the procurement organization gets value for money. He should also be responsible for the efficiency of the purchasing organization and for the probity of its dealing with suppliers. In larger departments the director should preferably have proven practical experience in the private sector.

9. A central focus for good purchasing practice is needed in central government. The reports proposes the establishment of a small central purchasing unit (CPU), to be headed by someone from the private sector. In addition to providing advice to departments, the CPU would also agree savings targets with them and report annually to the Prime Minister on progress in implementing the report.

10. The report makes some recommendations on the three agencies which took part in the review (Crown Suppliers, HMSO and CCTA). These are aimed at developing the relationship between the agencies and departments so that the former provide an adequate level of service to the latter. Ultimately the strategy could lead to departments being untied from the agencies.

11. The proposals in the report will help government obtain better value for money. At the same time they should help industry become more competitive. The conclusions confirm the principles of the Public Purchasing Initiative. They also show the importance of implementing the principles of the Financial Management Initiative in departments. Implementation of the recommendations will make a practical contribution to the development of the FMI.



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10 DOWNING STREET

From the Private Secretary

7 August 1984

Government Purchasing

The Prime Minister was grateful for Lord Gowrie's minute of 3 August about the Cabinet Office review of Government purchasing.

The Prime Minister agrees that Lord Gowrie should now circulate the papers more widely, under cover of a letter setting out the main issues for discussion. She further agrees that, once this has been done, a meeting should be arranged under her chairmanship, and we will be in touch with your office, and with the offices of those Ministers mentioned in the penultimate paragraph of Lord Gowrie's minute, to find a time. The Prime Minister would also wish Sir Robert Armstrong and Sir Robin Ibbs to be present.

I am sending copies of this letter to Margaret O'Mara (HM Treasury), Richard Hatfield (Cabinet Office) and to Sir Robin Ibbs.

David Barclay

Mrs Mary Brown,
Office of the Minister for the Arts.

NR

(1)
PRIME MINISTER

Government Purchasing

I attach a minute from Lord Gowrie about the review of Government purchasing recently completed by the Cabinet Office.

There are big savings to be made - up to £400 million ^{a year} not counting what might be saved on "war-like" purchasing. But these savings would come from taking a tougher and more commercial line with suppliers. So there will be protests from those parts of industry who have been doing well (perhaps too well) out of supplying the Government.

The report raises two machinery of government issues, on which Sir Robert Armstrong will be letting you have advice:-

- (i) The establishment of a Central Purchasing Unit.
- (ii) The implications for Central Purchasing agencies such as HMSO, Crown Suppliers and CCTA.

As the next step, Lord Gowrie recommends a meeting under your chairmanship to discuss the report and its handling. The proposed attendance is:

+ Lord Gowrie
Chancellor of the Exchequer
Foreign Secretary
Home Secretary
Secretary of State for Defence
Secretary of State for Social Services
Secretary of State for the Environment
Secretary of State for Trade and Industry
Secretary of State for Transport
Sir Robert Armstrong
Sir Robin Ibbs

Content for us to set up such a meeting, and for Lord Gowrie to circulate the papers to colleagues?

6 August, 1984.

Yes ml
DMS